IN THE CHANCERY COURT FOR THE STATE OF TENNESSEE
TWENTIETH JUDICIAL DISTRICT, DAVIDSON COUNTY, PART IV

VODAFONE AMERICAS HOLDINGS, INC. and SUBSIDIARIES,	)	
Plaintiffs,	)	
vs.	)	**CASE NO. 07-1860-IV**
RICHARD H. ROBERTS,[1] Commissioner of Revenue, State of Tennessee,	)	
Defendant.	)	

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MEMORANDUM AND ORDER

In this tax refund case, one of two foreign general partners in a general partnership claimed (in constitutional and statutory terms) that it had no liability for Tennessee franchise and excise taxes because it only has a 45% interest in the partnership and it did not have control of the partnership's day-to-day operations. Additionally, this 45% general partner is claiming that the taxing authority abused its discretion in imposing a variance and erred in calculating this vigorously contested proposed tax liability. The taxing authority counters, urging that the tax liability at issue passes through to the general partners; that the challenged variance fairly calculates the taxable business activity in Tennessee; and that the variance is appropriately tailored to avoid substantial "nowhere income."

On August 16, 2007, Vodafone Americas Holdings, Inc. ("VAHI") and Subsidiaries (collectively referred to as "Vodafone" or "Plaintiffs"), the 45% general partner mentioned above, filed suit against Tennessee's Commissioner of Revenue

[1] Richard H. Roberts, the current Commissioner of the Tennessee Department of Revenue, was automatically substituted as a party when he took office. *See* Tenn. R. Civ. P. 25.04(1).

("Commissioner" or "Defendant"), seeking a refund of franchise and excise taxes in the principal amount of $13,645,288, together with interest, attorney's fees and expenses. On December 23, 2008, Plaintiffs filed an Amended Complaint seeking a refund in the same amount, but raising for the first time in Count Eight that a cost-of-performance analysis should apply. Plaintiffs' Amended Complaint also added more detail in describing the claims. Vodafone is seeking a refund for the period of January 1, 2002 through March 31, 2006 (the "Relevant Period").

Under Tennessee law, any tax liability attributable to a business operating as a general partnership flows through to the general partners. The general partnership itself is not taxed. In other words, the general partners, not the partnership, are the taxpayers. For the reasons stated in the November 5, 2012 Order Granting a Partial Summary Judgment, the Court has concluded that Vodafone is subject to Tennessee's franchise and excise taxes.

Originally, Vodafone used the apportionment method that was later embodied in the Commissioner's variance. Vodafone, however, filed an Amended Complaint that sought a refund on the basis of the cost-of-performance formula. After that, the Commissioner issued a variance, opining that the cost-of-performance methodology did not fairly represent Vodafone's business activity in Tennessee.

The parties filed cross-motions for summary judgment, which were argued on September 13, 2012. At the conclusion of the hearing, the Court announced that it was granting summary judgment in favor of the Commissioner on the nexus issues and denying summary judgment on all remaining issues. On November 5, 2012, this ruling was memorialized in the Court's Order Granting a Partial Summary Judgment, a copy of which is attached and incorporated by reference in this Memorandum and Order as

Exhibit 1. As contemplated by the Order entered on December 17, 2012, this case was tried to the Court on March 5, 2013 on stipulations and a written evidentiary record. *See* Tenn. R. Civ. P. 43. The Parties' Joint Stipulation of Facts, filed on February 15, 2013, are fully incorporated by reference in this Memorandum and Order as Exhibit 2.

Facts

From January 1, 2002 through March 31, 2006 (the "Relevant Period"), Vodafone Americas Holdings, Inc. ("VAHI") had its principal place of business and commercial domicile in Walnut Creek, California. *See* Amended Complaint ("Compl.") ¶ 1. VAHI is a wholly owned, indirect subsidiary of Vodafone Group PLC, a British mobile phone operator headquartered in Newbury, Berkshire, England. *See* Compl. ¶ 1. Vodafone Group PLC is the largest mobile telecommunications network company in the world, with ownership interests in 27 countries across five continents. *See* Pls.' Resps. to Def.'s First Set of Interrogs. and Doc. Reqs. for Pls. ("Pls.' First Resps.") No. 2(a).

Aside from activities necessary as a result of and directly related to being publicly traded on the New York Stock Exchange, Vodafone Group PLC's activities in the United States during the Relevant Period were limited to its ownership interest – through the various entities that comprise Plaintiffs – a 45% interest in the Cellco Partnership ("Cellco"). *See* Pls.' First Resps. No. 2(a); Transcript of Deposition of Megan Doberneck ("Doberneck Dep.") 30:21-24, 49:22-51:1, 53:20-54:25. Cellco operates a telecommunications business known as "Verizon Wireless." Pls.' First Resps. No. 2(a). Cellco is a partnership governed by the Delaware Revised Uniform Partnership Act, Title 6 of the Delaware Code, Section 15-101, *et seq.*, the Cellco Partnership Amended and Restated Partnership Agreement (the "Partnership Agreement") and amendments thereto, and the Alliance Agreement between Vodafone and Verizon Communications ("Alliance

Agreement"). *See* Pls.' First Resps. No. 2(a). Together, the entities that comprise the Vodafone Plaintiffs own 45% of Cellco, and Verizon Communications owns the majority and controlling 55% share of Cellco. *See* Pls.' First Resps. No. 2(a).

The relationship between Plaintiffs and Verizon Communications as partners to Cellco is governed and controlled by the Partnership Agreement and the Alliance Agreement. *See* Pls.' First Resps. No. 2(a). Under the terms of the Alliance Agreement, Vodafone's interest in Cellco is established at 45%, and Verizon Communications is provided a majority 55% share. *See* Pls.' First Resps. No. 2(a); Alliance Agreement § 2.8. The Partnership Agreement created a Board of Representatives for Cellco with functions similar to those of a board of directors of a publicly-traded Delaware corporation. *See* Pls.' First Resps. No. 2(a); Partnership Agreement § 3.2. The Partnership Agreement states: "the Board of Representatives shall function in a manner comparable to that of a board of directors of a publicly traded, Delaware corporation." Partnership Agreement § 3.2. As provided in the Partnership Agreement, management of Cellco rests exclusively with the Board of Representatives and not with its partners. *See* Partnership Agreement § 3.2.

The Cellco Board of Representatives is responsible for managing the business of Cellco, and at all times, Verizon Communications – not Vodafone – was in control of the majority of seats on the Board. *See* Pls.' First Resps. No. 2(a); Partnership Agreement §§ 3.2, 3.3; Amendment to Partnership Agreement ¶ 1. The partners to the Partnership Agreement are expressly prohibited from acting in the name of or on behalf of Cellco. *See* Partnership Agreement § 3.1. The Partnership Agreement states:

> [N]o Partner shall take any action in the name of or on behalf of [Cellco], including without limitation assuming any obligation or responsibility on behalf of [Cellco], unless such action, and the taking thereof by such Partner,

> shall have been expressly authorized by the Board of Representatives or shall be expressly and specifically authorized by this Agreement.

Id. The Partnership Agreement also states: "No Partner shall have any authority to act for, or to assume any obligation or responsibility on behalf of, any other Partner or [Cellco], except as expressly authorized in this Agreement or as authorized by the Board of Representatives." Partnership Agreement § 1.11.

The Partnership Agreement originally provided for a Board of Representatives comprised of seven members, of which Vodafone had the right to appoint three and Verizon Communications had the right to appoint four. *See* Partnership Agreement § 3.3(a). Through an amendment to the Partnership Agreement dated July 24, 2003, the number of members on the Cellco Board of Representatives was increased to nine, with Vodafone having the right to appoint four and Verizon Communications having the right to appoint five. *See* Amendment to Cellco Partnership Amended and Restated Partnership Agreement ("Amendment to Partnership Agreement") ¶ 1. At all times, Verizon Communications was in control of the majority of seats on the Cellco Board of Representatives. *See* Amendment to Partnership Agreement ¶ 1; Partnership Agreement § 3.3(a).

At all times during the Relevant Period, nearly all Board of Representatives' decisions required a majority vote from the Board members. *See* Partnership Agreement § 3.3. The only exceptions to the rule that Cellco Board of Representatives' decisions required a majority vote from the Board members were certain limited veto rights expressly granted in Section 4.1 of the Partnership Agreement. *See* Partnership Agreement § 4.1. Because Vodafone held a minority of seats on the Cellco Board of Representatives, and because almost all votes required a simple majority of the board

members present, Vodafone could take no action with regard to Cellco or its business operations (other than the veto rights provided in Section 4.1) without a consenting vote from Verizon Communications. *See* Partnership Agreement §§ 3.3, 4.1; Doberneck Dep. 59:11-25.

The Verizon Wireless network is not compatible with the GSM technology used in Vodafone's networks throughout the world. *See* Pls.' First Resps. No. 2(a); Doberneck Dep. 65:2-62:21. Because of the differences in technologies, and because Vodafone is unable to control the operations of the Verizon Wireless business, there is no customer integration or crossover between Verizon Wireless' telecommunications business in the United States and Vodafone's telecommunications business conducted in the rest of the world. *See* Pls.' First Resps. No. 2(a); Doberneck Dep. 65:2-65:21. Due to the incompatibility of networks, when Vodafone's customers travel to the United States, they use – and pay for – the telecommunications services offered by one of Vodafone's and Verizon Wireless' competitors, rather than the network operated by Verizon Wireless. *See* Pls.' First Resps. No. 2(a).

Plaintiffs filed Tennessee franchise and excise tax returns and paid Tennessee franchise and excise taxes for each year in the Relevant Period. *See* Pls.' First Resps. 6(a); Compl. ¶¶ 9-11. In Plaintiffs' original franchise and excise tax returns for the Relevant Period, Plaintiffs calculated their apportionment formula sales factor by sourcing to Tennessee any sales of Cellco's telecommunications services that were made to customers with a Tennessee billing address. *See* Pls.' First Resps. No. 14(c). After the Relevant Period, and as a result of a change in their tax and accounting personnel, Plaintiffs reviewed the manner in which they were filing returns in a number of states,

including Tennessee. *See* Doberneck Dep. 41:20-43:4, 88:14-89:12; Transcript of Deposition of Michael Stamm ("Stamm Dep.") 15:4-12.

Plaintiffs filed claims for refunds of the taxes they had paid for the Relevant Period, asserting no Tennessee franchise and excise taxes were due because Plaintiffs lacked the statutorily and constitutionally required business activity in Tennessee to be subject to the taxes. *See* Compl. ¶¶ 9-11; Exhs. A & C. Defendant denied Plaintiffs' refund claims in their entirety. *See* Compl. ¶¶ 9-10; Exhs. B & D. After receiving Defendant's denial of their refund claims, and after receiving a waiver of the requirement for filing additional refund claims (on the same bases, but for additional years and entities) before filing suit, Plaintiffs filed this litigation to receive the refunds they claim for the Relevant Period. *See* Compl. ¶¶ 9-11.

Throughout the Relevant Period, Verizon Wireless engaged in the wireless voice and data business (cellphone business) in Tennessee and had an enforceable contract with customers with Tennessee billing addresses, the revenues from which contracts were included in the apportionment schedule provided to Vodafone by Verizon Wireless, from which Vodafone derived the numerators of the sales factors of the apportionment formulas used in the original F & E returns filed by Vodafone. *See* OGPS, pp. 3-4. During the same period, more than ninety-five percent of Vodafone's income was comprised of its distributive share flowing from its forty-five percent general partnership interest in Cellco Partnership (Verizon Wireless). *See* Stip. Exh. 9, Doberneck Dep., p. 55, line 1 – p. 56, line 2, p. 58, lines 4-7; Stip. Exh. 12, Stamm Dep., p. 43, lines 25 – p. 45, line 6. Vodafone filed amended F & E returns and requests for refunds for the entire Relevant Period asserting that no Tennessee F & E taxes were due because it lacked

nexus. The Department denied all of the requests for refunds, and Vodafone timely filed this refund action for the Relevant Period. *See* Stip. Facts 14-17.

At a partners meeting in May 2008, Vodafone became acquainted with a cost-of-performance sourcing methodology study that had been performed for Verizon Wireless or Verizon Communications by PricewaterhouseCoopers ("PwC") in New York. Vodafone then hired PwC in Denver to assist it in developing a cost-of-performance study for Vodafone. *See* Stip. Exh. 12, Stamm Dep., p. 15, line 18 – p. 22, 1.4; Stip. Exh. 17, Memo from Todd Roberts (Exh. 10 to Doberneck Dep.); Stip. Exh. 21, COP Powerpoint May 2008 (Stamm Dep. Exh. 2); Stip. Exh. 20, PwC letter to Greco dated 12/5/08 (Stamm Dep. Exh. 1). In December 2008 Vodafone filed an Amended Complaint, adding Count Eight, which advanced for the first time the use of a cost-of-performance sourcing methodology to source outside of Tennessee receipts from sales of wireless telecommunications services to customers with Tennessee billing address. *See* Stip. Fact 8. In their original F & E returns, Vodafone had calculated their apportionment formulas by sourcing to Tennessee receipts from any sales of wireless telecommunications services provided to customers with Tennessee billing addresses. *See* Stip. Fact 11.

In its Amended Complaint, in the alternative to a complete refund based upon lack of nexus, Vodafone sought a substantial refund based on cost-of-performance sourcing, as opposed to the sourcing in its original returns based upon customer billing address. *See* Stip. Fact 18. After *BellSouth Advertising & Publishing Company v. Chumley,* 308 S.W.3d 350 (Tenn. Ct. App. 2009) *perm. app. denied,* March 1, 2010, ("*BAPCO*") was decided, then-Commissioner Farr, by letter dated May 21, 2010, issued a variance pursuant to the statutory authority of Tenn. Code Ann. §§ 67-4-2014(a) & 67-4-

2112(a).[2] *See* Stip. Exh. 14, Variance Letter (Doberneck Dep., Exh.3); Stip. Fact 19. The variance required Vodafone to continue to source to Tennessee receipts from sales or wireless services to customers with Tennessee billing addresses. *See* Stip. Facts 20 & 21.

Under the cost-of-performance methodology relied upon by Vodafone, for the Relevant Period the cumulative numerator of the sales factor of the apportionment formula would fall more than $1,200,000,000, from $1,357,566,794 to $150,896,965, an 89% difference from the billing-address sourcing used by Vodafone in its original F & E returns. *See* OGPSJ, p. 4; Stip. Exh. 24, Vodafone Numerator Chart. Vodafone's receipts from customers with Tennessee billing addresses, which receipts have not been included in the numerator of the sales factor through use of its cost-of-performance sourcing methodology, have not been reported to or claimed by any other jurisdiction. *See* Stip. Exh. 5, Plaintiffs' Responses to Defendant's Third Interrogatories, Interrogatory 4. After application of its cost-of-performance sourcing methodology, the numerator of the sales factor of the apportionment formula in Vodafone's F & E returns would include only sales of tangible personal property, and no revenues from its delivery of wireless services to customers in Tennessee. *See* Stip. Exh. 12, Stamm Dep., p. 39, line 21 – p. 40, line 6. As of January 30, 2012, Vodafone has filed refund claims based upon a nexus theory similar to the one advanced in this case in 12 other states and upon a similar cost-of-performance theory in 11 other states (18 total states, including Tennessee). *See* Stip. Exh. 16, Letter from Steve Jasper to Talmage Watts dated February 1, 2012.

[2] These two variance statutes are virtually identical; Tenn. Code Ann. § 67-4-2014(a) applies to excise taxes and Tenn. Code Ann. § 67-4-2112(a) applies to franchise taxes.

Variance Letter

After litigating this case for nearly three years, by letter dated May 21, 2010, then-Commissioner of Revenue Reagan Farr notified Plaintiffs of the imposition of a variance. The body of this variance letter provided, in its entirety, as follows:[3]

> [1.] The listed business entities and their parent, Vodafone Americas Holdings, Inc. (collectively the "Taxpayers") are presently in litigation with this Department concerning refund claims filed for the tax years ended during the period beginning January 1, 2000, and ending March 31, 2006.
>
> [2.] The Taxpayers are, directly or indirectly, general partners in Cellco Partnership, which is a general partnership that does business in Tennessee under the name "Verizon Wireless." Under Tennessee's statutory scheme, franchise/excise taxes are not imposed against general partnerships. In effect general partnerships are disregarded, and franchise/excise taxes are imposed on their partners, provided that such partners are taxable business entities.
>
> [3.] On their original franchise/excise tax returns filed with this Department, the Taxpayers used the pay-per-use or primary-place-of-use ("PPU") methodology to determine the gross receipts to be included in the numerators of the gross receipts factors of each of their apportionment formulas. Under the PPU methodology the Taxpayers sourced their earnings according to the locations of their cellphone customers.
>
> [4.] Now, through their refund claims and the resulting litigation, the Taxpayers assert that they are entitled to use a methodology that is different from the PPU methodology originally used to compute receipts. One of the principal theories that the Taxpayers advance in support of their refund claims asserts that the numerator of each Taxpayer's gross receipts factor in its apportionment formula should be determined under the provisions of Tenn. Code Ann. §§ 67-4-2012(i) and 67-4-2111(i), sometimes referred to as the cost-of-performance ("COP") methodology. Use of the so-called COP methodology, at least as the Taxpayers have calculated it, would result in a substantial reduction in the gross receipts that each Taxpayer would include in the numerator of the receipts factor of its apportionment formula for each tax period. As a result, there would be a substantial reduction in each Taxpayer's franchise/excise tax liability.

[3] For purposes of this Memorandum and Order, the Court has sequentially numbered all the paragraphs (1-15) in the Commissioner's variance letter. The Court notes, however, that the Commissioner's letter contains fifteen un-numbered paragraphs.

[5.] I have given careful study to information produced by the Taxpayers that shows the difference in the COP and PPU methodologies when applied in determining gross receipts to be included in the numerators of their apportionment gross receipts factors. The PPU methodology originally used by the Taxpayers sources receipts according to the places at which the Taxpayers' customers are located and where the cellphone services are provided. But the COP methodology proposed by the Taxpayers sources receipts according to the place where the taxpayers arguably incur the costs of providing services.

[6.] The PPU 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. In this context, it is not reasonable to say that receipts from a Tennessee customer should be attributed to another jurisdiction because, for example, a call that he or she made was routed through some facilities in other jurisdictions or more of the Taxpayers' general overhead costs are incurred in other jurisdictions than in Tennessee.

[7.] Under the PPU method, it is easy to determine the state to which receipts from services provided to the Taxpayers' cellphone customers should be attributed because a receipt from a customer residing in a particular state is attributed to that state. To verify whether a receipt has been correctly attributed to a particular state, it is only necessary to determine the state in which the cellphone customer from which the payment was received is located.

[8.] The COP 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 proportion 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 COP method that the Taxpayers propose.

[9.] Costs 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. When attempting 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.

[10.] I am aware of an October 30, 2009, memorandum prepared by PricewaterhouseCoopers to explain the COP methodology that the Taxpayers proposed to employ. It appears from that memorandum that the Taxpayers' calculations under their COP methodology include their costs for rendering all of their services to their customers everywhere, rather than being limited to their costs for rendering services in Tennessee. While the latter would doubtless be a complex calculation, it may well be that a reliable calculation under the COP method would produce a far different result than the Taxpayers claim.

[11.] According to the PricewaterhouseCoopers Memorandum, the states in which these Taxpayers had higher costs of performance than Tennessee were California, Georgia, and New Jersey, none of which follows a COP methodology. Because the statutes of some states in which Taxpayers do business do not employ a COP methodology, application of the COP method as calculated by the taxpayers would result in many millions of dollars of their earnings from Tennessee residents escaping their fair share of taxation in Tennessee or anywhere else. As calculated by the Taxpayers, application of the COP methodology would mean that the overwhelming majority of these Taxpayers' earnings would not be captured in any other state. According to information provided by the Taxpayers, the receipts that escape taxation in any state when the Taxpayers apply their calculation of the COP methodology to the years in litigation exceed $1 billion.

[12.] It is clear to me that application of the COP methodology when determining gross receipts to be included in the numerators of the Taxpayers' gross receipts factors in their apportionment formulas would not fairly represent the extent of business activities conducted in Tennessee by the Taxpayers as a result of their direct and indirect general partnership interest in Cellco Partnership. Use of the COP methodology allows the Taxpayers, through their direct and indirect general partnership interests in Cellco Partnership, to derive substantial receipts from Tennessee markets without such receipts being accounted for in the Tennessee receipts factors of their franchise/excise tax apportionment formulas and without such receipts being recognized in other taxing jurisdictions.

[13.] Accordingly, I have decided to require a variance for the tax years under litigation and for all subsequent tax years pursuant to the authority granted me by Tenn. Code Ann. §§ 67-4-2014 and 67-4-2112.

[14.] Under the variance imposed, the Taxpayers will be required to determine the gross receipts to be included in the numerators of the apportionment formula gross receipts factors for tax years in litigation and for all subsequent tax years by using the PPU methodology that they originally used when filing their franchise/excise tax returns for the tax years in litigation. I believe that use of the PPU method is necessary to

> fairly represent the extent of the business activities that the Taxpayers conduct in Tennessee through their direct and indirect general partnership interests in Cellco Partnership.
>
> [15.] The variance requirements described above will continue in effect so long as the circumstances justifying a variation remain substantially unchanged or until changed or discontinued by this Department, whichever occurs first.

Trial Exhibit 14.

The Commissioner did not put great emphasis on the regulations in articulating his reasons for the variance. He put most of his emphasis on the statutory standard requiring him to demonstrate that Vodafone's cost-of-performance approach did not fairly represent Vodafone's business activity in Tennessee. A review of the variance letter (Trial Exhibit 14), therefore, yields the following points:

1. Vodafone's original franchise/excise tax returns used the primary-place-of-use ("PPU") methodology, sourcing their earnings to the states where their cell phone customers were located; (¶ 3)

2. Vodafone's specific calculation of the cost of performance, which the Commissioner challenged, resulted in a substantial reduction of Vodafone's gross receipts that they would use in the formula; (¶ 4)

3. After carefully studying the details of Vodafone's methodologies as presented to him, the Commissioner could not determine that that the receipts were attributed to the actual place where Vodafone incurred the costs of providing services; (¶ 5)

4. The PPU method was readily substantiated, while the cost-of-performance was not and was potentially subject to arbitrary assignment of costs to particular states; (¶¶ 6-9)

5. The particular calculations offered included Vodafone's costs everywhere and did not capture Tennessee-specific costs, resulting in over a billion dollars in taxable receipts from Tennessee customers not being taxed in Tennessee or any other state; (¶¶ 10-11)

6. The cost-of-performance methodology, coupled with their direct and indirect partnership interests in Cellco partnership, allows these particular taxpayers to shift over a billion dollars in previously taxable receipts in such a way that they are not captured by Tennessee or any other state; (¶ 12) and

7. Given all of the foregoing, the Commissioner concluded that the cost-of-performance methodology, as proposed by Vodafone, did not fairly reflect Vodafone's business activity in Tennessee and, conversely, that use of what the Commissioner characterized as the PPU method would fairly represent the extent of Vodafone's business activities in Tennessee. (¶¶ 12 & 14).

Expert Proof

Both sides presented the testimony of distinguished experts on the variance question. Professor John A. Swain, a law professor at the University of Arizona Rogers College of Law, testified on Vodafone's behalf. Professor Swain concluded that "[t]here are no unusual circumstances to justify the imposition of the Variance" and that the problems that the Commissioner articulated in support of the variance "apply equally to all providers of telecommunication services." Trial Exh. 7, pp. 2 & 3. Additionally, Professor Swain opined that the Commissioner "cannot . . . enact the broader, industry-wide policy change effectuated by the Variance on a case-by-case basis through the imposition of a variance." *Id.* at 4.

Professor Swain concluded that the Commissioner applied the variance retroactively and that the Commissioner was not authorized through the variance procedure to prevent "so-called 'nowhere income.'" *Id.* at 4-5. He opined that "[t]he cost-of-performance methodology reaches a fair result when applied to Vodafone by taking into account all of the costs that are related to providing Verizon Wireless services." *Id.* Professor Swain concluded that the Commissioner abused his discretion in all of the foregoing respects given that "there were no unusual circumstances present that would justify the need to deviate from the legislatively chosen methodology." *Id.* at 4-6.

The Commissioner's expert, Benjamin F. Miller, is a distinguished state tax lawyer with substantial legal, regulatory, and other pertinent experience. Mr. Miller

opined that "two fundamental principles of UDITPA are: (1) that no income should be assigned to more than one State; and (2) that no income should escape taxation, such income frequently being referred to as 'nowhere income.'" Trial Exh. 8, p. 2 (footnote with citation omitted). Mr. Miller agreed with the Commissioner's conclusion in his variance letter, opining that "[a]doption of the taxpayers' proposal would result in none of the Tennessee sales being attributed to any state and would result in a substantial portion of their income escaping any state taxation." *Id.* at 13.

Additionally, Mr. Miller assigned some weight to the fact that Vodafone had initially used the approach reflected in the Commissioner's variance:

> 8. The taxpayers filed their original returns for all years for which they have filed suit assigning the sales at issue based upon the billing address of their customers as Tennessee sales. This is evidence, at least initially, that the taxpayers did not believe that their method of filing unfairly represented their activities in Tennessee. If they believed that this did not fairly represent their activities in Tennessee they could have requested a variance.

Id. at 13-14. Mr. Miller opined that the Commissioner's decision to adopt the approach tied to Tennessee customers was reasonable and appropriate:

> 6. At the very least the reasonableness of the Commissioner's decision is evidenced by the fact that the taxpayers filed their original returns in that manner. There is no retroactivity involved in the Commissioner's decision. Tennessee accepted the returns as filed. The taxpayer raised the issue by filing claims for refund. It was only when claims for refund were filed that the Commissioner had occasion to consider the method sought by the taxpayer. The Commissioner reviewed the material submitted by the taxpayer, and only after considering that information did he issue a ruling invoking UDITPA section 18. That was the first point in time when the Commissioner needed to address the question.

Id. at 16.

Discussion and Conclusions of Law

Applicable Tenets of Construction

At the outset, the Court recognizes its duty to follow basic tenets of statutory construction as announced by our appellate courts:

> Our duty in construing statutes is to ascertain and give effect to the intention and purpose of the legislature. Legislative intent is to be ascertained whenever possible from the natural and ordinary meaning of the language used, without forced or subtle construction that would limit or extend the meaning of the language.
>
> When the statutory language is clear and unambiguous, we must apply its plain meaning in its normal and accepted use, without a forced interpretation that would limit or expand the statute's application. Where an ambiguity exists, we must look to the entire statutory scheme and elsewhere to ascertain the legislative intent and purpose. The statute must be construed in its entirety, and it should be assumed that the legislature used each word purposely and that those words convey some intent and have a meaning and a purpose. The background, purpose, and general circumstances under which words are used in a statute must be considered, and it is improper to take a word or a few words from its context and, with them isolated, attempt to determine their meaning.

Eastman Chem. Co. v. Johnson, 151 S.W.3d 503, 507 (Tenn. 2004) (internal quotations and citations omitted). This Court, therefore, looks to the statutory language as its first order of business. *See CAO Holdings, Inc. v. Trost,* 333 S.W.3d 73, 85-86 (Tenn. 2010). After that, if other rules of construction apply, the Court follows them.

Courts are required to liberally construe statutes that impose a tax in favor of the taxpayer and strictly construe them against the taxing authority. *See Eastman Chem. Co.,* 151 S.W.3d at 507. "[W]here there is doubt as to the meaning of a taxing statute, the doubt must be resolved in favor of the tax payer." *Commercial Standard Ins. Co. v. Hixson,* 133 S.W.2d 493, 494 (Tenn. 1939). This construction, however, must be fair and give effect to the language of the statute. *See International Harvester Co. v. Carr,* 466 S.W.2d 207, 214 (Tenn. 1971); *United Inter-Mountain Tel. Co. v. Moyers,* 426 S.W.2d

177, 181 (Tenn. 1968). Unless the text of a revenue statute requires otherwise, courts are expected to give the words in the statute their natural and ordinary meaning and to enforce revenue statutes as written. *See Eastman Chem. Co.*, 151 S.W.3d at 507; *Stratton v. Jackson*, 707 S.W.2d 865, 866 (Tenn. 1986).

Courts should consider the natural and ordinary meaning of words in a revenue statute, unless the statutory language requires a different approach. *See Eastman Chem. Co.*, 151 S.W.3d at 507. When the statute's purpose is clear from the text of the statute, the language should be enforced as written. *See Stratton*, 707 S.W.2d at 866. There instances, however, when courts should use a more context-sensitive approach:

> A statute's meaning is derived, not from considering the separate meaning of each individual word in a statute, but from considering the entire statute as a whole in light of its general purpose. *See State v. Flemming*, 19 S.W.3d. 195, 197 (Tenn. 2000); *First Nat'l Bank of Memphis v. McCanless*, 186 Tenn. 1, 8, 207 S.W.2d 1007, 1009 (1948). Thus, rather than "'mak[ing] a fortress out of the dictionary,'" *Crown Enters., Inc. v. Woods*, 557 S.W.2d 491, 493 (Tenn. 1997) (quoting *Cabell v. Markham*, 148 F.2d 737, 739 (2d Cir. 1945)); *cf. Western Pipe Line Constructors, Inc. v. Dickinson*, 203 Tenn. 248, 257, 310 S.W.2d 455, 459-60 (1958), the courts' role is to ascertain and give the fullest possible effect to the General Assembly's intent and purpose without unduly restricting the statute's application or to expand its application beyond its intended scope. *In re Estate of Davis*, 308 S.W.3d 832, 837 (Tenn. 2010); *Seals v. H & F, Inc.*, 301 S.W.3d 237, 242 (Tenn. 2010).

CAO Holdings, Inc. v. Trost, 333 S.W.3d 73, 86 (Tenn. 2010).

The Commissioner's Variance

Generally speaking, the Commissioner's statutory and regulatory authority to issue variances is both narrow and discretionary. *See BellSouth Adver. & Publ'g Corp. v. Chumley*, 308 S.W.3d 350 (Tenn. Ct. App. 2009)("*BAPCO*"); *American Bemberg Corp. v. Carson*, 219 S.W.2d 169 (Tenn. 1949). One of the variance statutes which applies here, Tenn. Code Ann. § 67-4-2014(a), reads as follows:

(a) If the tax computation, allocation or apportionment provisions of this part or chapter 2 of this title do not fairly represent the extent of the taxpayer's business activity in this state, or the taxpayer's net earnings, the taxpayer may petition for, or the department through its delegates may require, in respect to all or any part of the taxpayer's business activity, if reasonable:

(1) Separate accounting;
(2) The exclusion of any one (1) or more of the formula factors;
(3) The inclusion of one (1) of more additional apportionment formula factors that will fairly represent the taxpayer's business activity in this state;
(4) The use of any other method to source receipts for purposes of the receipts factor or factors of the apportionment formula numerator or numerators; or
(5) The employment of any other method to effectuate an equitable computation, allocation and apportionment of the taxpayer's net earnings or losses that fairly represents the extent of the business entity's activities in Tennessee.

Id.

Under the statute, the Commissioner has discretion to choose a narrow or sweeping change in the standard apportionment formula for a specific situation once he has decided to issue a variance. *See* Tenn. Code Ann. § 67-4-2014(a)(1)-(5). In other words, once the Commissioner has used his narrow discretion to determine that the taxpayer's use of the standard formula does not fairly represent the extent of the taxpayer's business activity in the state, then the Commissioner's discretion to choose a different methodology for a particular taxpayer is, by the language of the statute, considerably broader. The pertinent regulation anticipates that the variance statute would "permit a departure from the allocation and apportionment provisions only in limited and specific cases." Tenn. Comp. R. & Regs. 1320-06-1-.35(1)(a)(4). This same regulation provides that the Commissioner's variance power "may be invoked only in specific cases where unusual fact situations (which ordinarily will be unique and nonrecurring) produce

incongruous results under the apportionment and allocation provision contained in the Franchise and Excise Tax Law." *Id.*

In short, the Commissioner is permitted to issue a variance in a situation when application of the statutory formula would yield a result that does not "fairly represent the extent of the taxpayer's business activity in Tennessee," or the taxpayer's net earnings. *BAPCO,* 308 S.W.3d at 367. In examining the question of whether the "tax computation, allocation or apportionment provisions . . . fairly represent the extent" of the taxpayer's business activity or net earnings in Tennessee, Tenn. Code Ann. § 67-4-2014(a), the regulation provides that a variance or "a departure from the allocation and apportionment provisions" is permitted "only in limited and specific cases." *Id.* at 367. Additionally, the regulation anticipates that these "limited and specific cases" would be "where unusual fact situations . . . produce incongruous results[.]" *Id.* Parenthetically, the regulation provides that these unusual fact situations producing incongruous results are "ordinarily . . . unique and nonrecurring." *Id.* In *BAPCO*, the Court pointed out that use of the "ordinarily" qualifier permitted the Commissioner to issue a variance in circumstances that may not necessarily be "unique and nonrecurring." *BAPCO,* 308 S.W.3d at 367.

Here, although the details and reliability of Vodafone's specific methodology and calculations are disputed, it is undisputed that the statutory cost-of- performance method would apply to Vodafone's operations for the period in question if no variance had been issued. It is clear that the Commissioner has the burden of showing that the variance was properly issued. *See BAPCO*, 308 S.W.3d at 362. In *BAPCO*, the Court of Appeals acknowledged that the Commissioner may exercise discretion to vary the applicable statutory formula "when application of the formula does not fairly represent the taxpayer's business in the state." *Id.* at 365 (citation omitted). In this context, the Court

in *BAPCO* applied a reasonableness standard in examining the Commissioner's issuance of a variance. *See id.* at 367.

The Commissioner issued a variance after examining Vodafone's decision to change from the destination-based methodology it had previously used in Tennessee to the cost-of-performance method. This change resulted in over a billion dollars in previously taxable earnings no longer being taxable in Tennessee, which amounted to roughly an 89% reduction in an aspect of the formula that calculates tax liability. This was an unusual factual situation specific to Vodafone, particularly given the readily available before and after comparison. The Court holds that it was reasonable for the Commissioner to conclude that the cost performance methodology did not fairly reflect the extent of Vodafone's business activity in Tennessee. The Commissioner, after reviewing this unique situation, exercised his discretion to issue a variance. This was reasonable and did not constitute an abuse of discretion.

As far as the Court can determine, the Commissioner has not yet issued additional variances that would begin to show a trend toward a general application of his rationale to other companies that generate receipts in Tennessee, but incur most of their costs elsewhere. The fact that the Commissioner's decision and rationale could theoretically be applied in a more sweeping fashion to other companies and industries does not invalidate the variance for two basic reasons. First, the variance, by its terms, only applies to Vodafone. If the Commissioner begin to issue variances that apply to other companies using the same rationale, those decisions will have to be viewed on a case-by-case basis in light of a pattern that can be brought to a court's attention. Secondly, as evidenced by *BAPCO*, it appears that the uniform statute allowed for variances when the cost of performance formula "did not function very well for certain types of

businesses[.]" *BAPCO*, 308 S.W.3d at 365. In other words, the statutory and regulatory scheme applicable to variances anticipates that certain types of businesses, not just an isolated wholly unique circumstance, might properly trigger examination under Commissioner's variance authority – even though it is clear that the Commissioner's authority to actually issue variances is narrow.

Once the Commissioner properly exercised his narrow discretion to issue a variance, his authority to choose a new apportionment method was fairly broad under the express terms of the variance statute. The Commissioner's decision to use the PPU approach was within the statutory mandate on the logistics of an actual variance and was reasonable under the circumstances. The Commissioner's decision to use a completely different methodology than the cost-of-performance approach in this particular instance does not implicate any separation of powers problem because the statute itself gives the Commissioner broad authority to change the formula once his narrow discretion to grant a variance has been properly and reasonably exercised by virtue of the Commissioner's determination that Vodafone's utilization of the cost-of-performance analysis did not fairly represent Vodafone's business activity in Tennessee.

Vodafone relies heavily on the language of the regulation. Contrary to Vodafone's assertions, the Court concludes that the Commissioner reacted to Vodafone's "limited and specific" situation. It is an unusual situation given Vodafone's structure, its tax history in Tennessee, and the fact that a substantial percentage of its previously taxable income was no longer being taxed under the cost-of-performance approach. It would be an incongruous result for Vodafone to use the cost-of-performance approach as it proposed to use it under the circumstances of this case, especially given the statutory standard which identifies the taxpayer's business activity in Tennessee as the focal point.

The Court has simply applied the language of the variance statute and regulation to conclude that Vodafone's cost-of-performance approach does not fairly represent Vodafone's business activity in Tennessee. Given that it is clear that there is no duplication of tax liability resulting from the Commissioner's imposition of the variance, the Commissioner's variance here does not hinge on a showing that Vodafone's approach actually produces "nowhere income," even though the preponderance of the evidence supports such a finding.

As indicated above, variance regulations permit the Commissioner to grant a variance "only in limited and specific cases." Tenn. Comp. R. & Regs. 1320-06-1-.35(1)(a)(4). The Commissioner is permitted to grant a variance only in specific cases "where unusual fact situations (which ordinarily will be unique and nonrecurring) produce incongruous results" under the apportionment statutes. *Id.* The Court concludes that the Commissioner's decision to issue the variance here complies with these regulations and that the Commissioner has met his burden of proof here.

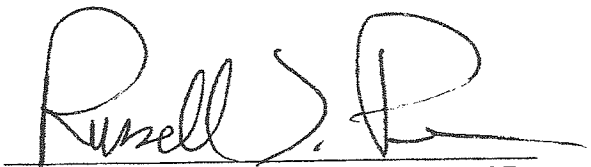
The Court agrees that this case is not really on all fours with *BAPCO*. The situation in *BAPCO* was factually different than the situation in this case. *BAPCO* is helpful, however, to the analysis here because it affirms that the Commissioner's variance decisions must be reasonable and follow the applicable statutory and regulatory language. *BAPCO* also reiterates that the scope of the Commissioner's discretion is narrow in determining whether a taxpayer's apportionment methodology fairly represents a taxpayer's business activity in the state. For the reasons stated in this Memorandum and Order, the Court concludes that the Commissioner properly followed *BAPCO* and the variance statutes and regulations.

Conclusion

Based on the foregoing, the Court HOLDS that the Commissioner met his burden of showing that the variance was properly issued and the Court DETERMINES that the Commissioner properly exercised his discretion under UDIPTA and the MTC regulations in issuing the variance. The variance was issued in response to a "tax computation, allocation or apportionment" which did not "fairly represent the extent of the taxpayer's business activity in the state." Tenn. Code Ann. §§ 67-4-2014(a) & 67-4-2112(a). The Court, therefore, DISMISSES Plaintiffs' Amended Complaint in its entirety, with prejudice, and hereby enters judgment in favor of Defendant, Richard H. Roberts, Commissioner of the Department of Revenue.

The Court determines that Defendant is entitled to an award of attorney's fees under Tenn. Code Ann. § 67-1-1803(d); those fees will be awarded separately upon Defendant's application after all appeals on the merits have been resolved and have otherwise become final. The Court determines, under Tenn. R. Civ. P. 54.02, that there is no just reason for delay and hereby DIRECTS the entry of final judgment in favor of Defendant and against Plaintiffs based on the ruling contained in this Memorandum and Order. The Court taxes court costs against Plaintiffs, Vodafone Americas Holdings, Inc. and its party subsidiaries, jointly and severally, for which execution may issue.

IT IS SO ORDERED.



RUSSELL T. PERKINS, CHANCELLOR

cc: Talmage M. Watts, Esq.
Michael D. Sontag, Esq.
Stephen J. Jasper, Esq.

EXHIBIT 1

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IN THE CHANCERY COURT FOR THE STATE OF TENNESSEE
20TH JUDICIAL DISTRICT, DAVIDSON COUNTY

VODAFONE AMERICAS HOLDINGS INC. AND SUBSIDIARIES,	)	RECEIVED NOV 0 2 2012 Dav. Co. Chancery Court
Plaintiffs,	)	
v.	)	No. 07-1860-IV
REAGAN FARR, Commissioner of Revenue, State of Tennessee,	)	
Defendant.	)	

FILED 2012 NOV -5 AM 9:38 DAVIDSON CO. CHANCERY CT.

ORDER GRANTING PARTIAL SUMMARY JUDGMENT

This matter came before the Court on September 13, 2012, at a hearing on cross-motions for summary judgment. Plaintiffs (collectively referred to as "Vodafone") and Defendant ("Commissioner") each filed motions for summary judgment on two distinct issues: (1) whether Vodafone has nexus in Tennessee and is doing business in this State so as to be subject to Tennessee franchise and excise taxes [the nexus issue], and (2) whether the Commissioner acted within his powers under Tenn. Code Ann. §§ 67-4-2014(a) and 67-4-2112(a) in imposing a variance that requires Vodafone to calculate the numerator of the receipts factor of its apportionment formula by sourcing sales of telecommunications services according to the billing addresses of customers to whom the services were provided, regardless of the jurisdiction in which the preponderance of the costs of performance were incurred as designated under Tenn. Code Ann. §§ 67-4-2012(i) and 67-4-2111(i) [the variance issue].

Both parties filed extensive memoranda, responsive memoranda, and reply memoranda. The parties also jointly submitted numerous stipulated exhibits, and each party was at liberty to submit its own exhibits and authorities. In consideration of all of the foregoing, and for the reasons set forth below, as to the nexus issue the Court grants the Commissioner's motion and denies Vodafone's motion, and as to the variance issue the Court denies the motions of both parties.

BACKGROUND

Vodafone seeks a refund of all franchise and excise taxes paid for tax years 2002 through 2006 ("relevant period").[1] Vodafone claims that it was not doing business in and had no taxable nexus with Tennessee during the relevant period. In the alternative, Vodafone seeks a substantial refund based upon use of a cost-of-performance sourcing methodology for determining the numerator of the receipts factor of its apportionment formula. In its original franchise and excise tax returns, Vodafone used the billing addresses of its customers for purposes of sourcing its receipts from sales of telecommunications services. Then, through its Amended Complaint, Vodafone first asserted its claim that it was entitled to a refund resulting from use of a sourcing methodology different from the one used in its original returns. Vodafone claims that the sourcing methodology used in its original returns was incorrect under Tennessee law and that it is required to use the cost-of-performance sourcing methodology provided in Tenn. Code Ann. §§ 67-4-2012(i) (excise tax) and 67-4-2111(i) (franchise tax). After Vodafone filed its Amended Complaint, the Commissioner issued a variance requiring Vodafone to continue to use the billing addresses of its customers to source sales of telecommunications services for the relevant period and thereafter. The

[1] Vodafone has abandoned its claims for refunds for tax years 2000 and 2001.

Commissioner asserts this authority under Tenn. Code Ann. §§ 67-4-2014(a) (excise tax) and 67-4-2112(a) (franchise tax), and Vodafone claims the variance imposed goes beyond the authority granted the Commissioner in those statutes.

Undisputed Facts Pertinent To This Order

Vodafone owns a 45% general partnership interest in Cellco Partnership ("Cellco"), a Delaware general partnership d/b/a Verizon Wireless. The other 55% general partnership interest is owned by subsidiaries of Verizon Communications Inc. ("Verizon"). Cellco is governed by the Cellco Partnership Amended and Restated Partnership Agreement, effective April 2000, and amendments thereto ("Partnership Agreement"). The business affairs of Cellco are managed by a Board of Representatives ("Board").

From the inception of Cellco in April 2000 through an amendment to the Partnership Agreement dated July 24, 2003, Vodafone (or its parent) appointed three and Verizon appointed four of seven members of the Cellco Board. After the amendment, Vodafone (or its parent) appointed four and Verizon appointed five of nine members of the Cellco Board. Pursuant to Section 3.5(b) of the Partnership Agreement, Vodafone has had the right to appoint and did appoint one significant officer of Cellco.

During the relevant period, Verizon Wireless continuously and systematically engaged in the wireless voice and data business (cellphone business) in Tennessee. Vodafone, as such, had no other presence in Tennessee. Verizon Wireless had enforceable contracts with customers with Tennessee billing addresses, the revenues from which contracts were included in the apportionment schedule provided to Vodafone by Verizon Wireless, from which Vodafone derived the numerators of the

receipts factors of the apportionment formulas of its original franchise and excise tax returns. Under the cost-of-performance methodology advanced by Vodafone, the cumulative numerator of the receipts factor of its apportionment formula for the relevant period would be reduced from $1,357,566,794 to $150,896,965.

Conclusions of Law

General partnerships are pass-through or disregarded entities for both federal and Tennessee tax purposes. Verizon Wireless is a general partnership and is not subject to Tennessee franchise and excise taxes at the partnership level. When Vodafone received its 45% distributive share from Verizon Wireless those funds had not been subjected to Tennessee franchise and excise taxes. This Court holds that a general partner of a general partnership doing business in Tennessee is present in Tennessee, is doing business in Tennessee, and meets all constitutional requirements for taxable nexus with Tennessee through the activities of the general partnership in Tennessee. Accordingly, Vodafone is subject to Tennessee's franchise and excise taxes, and the Commissioner's motion for summary judgment on the nexus issue is hereby GRANTED. Plaintiffs' motion for summary judgment on the nexus issue is DENIED.

As to the variance issue, the Court holds that a trial is required to resolve factual issues bearing on the propriety of the Commissioner's imposition of the variance at issue in this case under Tennessee law. Accordingly, the cross-motions for summary judgment on the variance issue are DENIED as to both parties.

The Court further notes that the parties have agreed that the merits of the actual cost-of-performance study that Vodafone alleges justifies the refund it claims in this case must be resolved at

trial. The Court thus expresses no opinion on that issue and, instead, finds that, if Vodafone prevails on the variance issue, there will also be a trial to determine the location of Vodafone's costs of performing the services at issue in this case and Vodafone's resulting franchise and excise tax liability.

For purposes of scheduling a trial on the variance issue and the issues identified in the prior paragraph, and to establish the procedure for addressing those issues at trial, this Court shall hold a pretrial conference with the parties at 10:00 a.m. on December 5, 2012.

It is so ORDERED.

RUSSELL T. PERKINS, CHANCELLOR

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EXHIBIT 2

IN THE CHANCERY COURT FOR THE STATE OF TENNESSEE,
20TH JUDICIAL DISTRICT, DAVIDSON COUNTY, TENNESSEE

VODAFONE AMERICAS HOLDINGS INC. and SUBSIDIARIES, Plaintiffs, v. REAGAN FARR, Commissioner of Revenue, State of Tennessee, Defendant.	)	No. 07-1860-IV

JOINT STIPULATION OF FACTS

Pursuant to this Court's Order entered December 17, 2012, the parties, by and through counsel, file this Joint Stipulation of Facts in connection with the trial of "the variance issue" in this case. The parties stipulate as follows:

1. Plaintiffs consist of Vodafone Americas Holdings Inc. ("VAHI") and a number of its subsidiaries, which filed Tennessee franchise and excise tax returns for the period January 1, 2002 through March 31, 2006 (the "Relevant Period").

2. For purposes of this litigation, there is no material difference between VAHI and its subsidiaries that, together, comprise the plaintiffs, which will be referred to herein collectively as "Vodafone" or "Plaintiffs."

3. During the Relevant Period, VAHI had its principal place of business and commercial domicile in Walnut Creek, California.

4. VAHI is an indirect, wholly owned subsidiary of Vodafone Group Plc, a British mobile phone operator headquartered in Newbury, Berkshire, England.

5. Vodafone Group Plc is a mobile telecommunications network company, with ownership interests in 27 countries across five continents.

6. Aside from activities necessary as a result of and directly related to being publicly traded in the United States, Vodafone Group Plc's activities in the United States during the Relevant Period were primarily related to its ownership – through the various entities that comprise Plaintiffs – of a minority interest in the Cellco Partnership ("Cellco").

7. Cellco operates its telecommunications business under the trade name "Verizon Wireless." Cellco sells and provides telecommunication services to its customers through Verizon Wireless.

8. Verizon Wireless (Cellco) is the industry-leading wireless service provider in the United States. Verizon Wireless offers wireless voice and data services across one of the most extensive networks in the United States.

9. Cellco's telecommunication service customers include customers with billing addresses in Tennessee and in each of the other states.

10. Plaintiffs filed Tennessee franchise and excise tax returns for each year in the Relevant Period and paid Tennessee franchise and excise taxes in accordance with those returns.

11. In Plaintiffs' original franchise and excise tax returns for the Relevant Period, Plaintiffs calculated their apportionment formula sales factor by sourcing to Tennessee any sales of Cellco's telecommunication services that were made to customers with a Tennessee billing address.

12. After the Relevant Period, and as a result of a change in their tax and accounting personnel, Plaintiffs reviewed the manner in which they were filing returns in a number of states, including Tennessee.

13. Plaintiffs filed claims for refunds of franchise and excise taxes they had paid for the Relevant Period.

14. In the refund claims Plaintiffs filed for the Relevant Period, Plaintiffs asserted that no Tennessee franchise and excise taxes were due because Plaintiffs lacked the statutorily and constitutionally required business activity in Tennessee to be subject to the taxes.

15. Defendant denied Plaintiffs' refund claims in their entirety.

16. After receiving Defendant's denial of their refund claims, and after receiving a waiver of the requirement for filing additional refund claims (on the same bases, but for additional years and entities) before filing suit, Plaintiffs filed this litigation.

17. In this litigation, Plaintiffs sought a full refund of all franchise and excise taxes Plaintiffs paid for the Relevant Period based on the same arguments asserted in their refund claims.

18. In addition, and in the alternative, Plaintiffs sought a refund of the Tennessee franchise and excise taxes they had paid for the Relevant Period in an amount equal to the difference between the amount Plaintiffs had paid as a result of calculating their liability by sourcing sales of Cellco's telecommunications services to the billing addresses of Cellco's customers and the amount that would be owed by sourcing sales of Cellco's services according to Plaintiffs' calculation of the location at which the preponderance of costs of performance were incurred under the methodology set forth in Tenn. Code Ann. §§ 67-4-2012(i) and 67-4-2111(i). It is Defendant's position that sourcing sales by using the cost of performance methodology Vodafone relies upon for this refund claim would fail to fairly reflect the extent of Vodafone's (through Verizon Wireless) business activity in Tennessee during the Relevant Period.

19. By letter dated May 21, 2010 (the "Variance Letter"), then-Commissioner of Revenue Reagan Farr notified Plaintiffs of his decision to impose a variance pursuant to Tenn. Code Ann. §§ 67-4-2014(a) and 67-4-2112(a). It is Plaintiffs' position that Commissioner Farr abused his discretion when he issued the Variance Letter and imposed the variance on Plaintiffs.

20. The variance imposed through the Variance Letter requires Plaintiffs to calculate their Tennessee apportionment formula sales factor for the Relevant Period and all subsequent years by using a primary-place-of-use methodology.

21. As stated in the Variance Letter, the primary-place-of-use methodology required Plaintiffs to source sales of Cellco's telecommunication services "according to the locations of their cellphone customers." Elsewhere in the Variance Letter, the primary-place-of-use methodology was described as sourcing receipts "according to the places at which the Taxpayers' customers are located and where the cellphone services are provided."

Respectfully submitted,

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