

Michigan's New Corporate Income Tax — The Road Ahead

by Lynn A. Gandhi and June Summers Haas

A Vow to Abolish the Michigan Business Tax

In 2010, as the gubernatorial election in Michigan began in earnest, Rick Snyder, a candidate for the Republican nomination, pledged to abolish the Michigan Business Tax (MBT). Snyder, a successful businessman, believed that to improve the business climate in Michigan, it was necessary to eliminate the MBT, a complicated and unique tax, which was top heavy with specialized incentives and credits.

At the time, several proposals were floating around Lansing to reduce the effective tax rate on businesses, including eliminating the MBT surcharge, eliminating the modified gross receipts levy under the MBT, and reducing the effective rate of the MBT. In illuminating his differences from the Granholm administration, Rick Snyder declared he would not tinker with the MBT. Rather, he said its elimination would be crucial to remaking the state.

Governor Snyder won by a wide margin, swept into office by the deep dissatisfaction felt by Michigan residents as one of the states hardest hit by the recession. Vowing to introduce a new tax regime and a two-year budget plan well before the required June 1, 2011 deadline, Governor Snyder appointed as the state's new Treasurer the former Speaker of the House, Andy Dillon, a Democrat who had been instrumental in the passage of the MBT. Treasurer Dillon was now to oversee the replacement of the MBT with a new tax regime.

In late spring of 2011, as part of his proposed budget,¹ Governor Snyder revealed his tax plans. The MBT was to be replaced with a simple corporate income tax at the rate of 6 percent. Only Subchapter C corporations would be subject to the tax; there would be no corporate level tax on other forms of entity. In addition, significant changes were proposed to the Individual Income Tax Act (IITA), placing more of the revenue burden on Michigan citizens. While the IITA rate was not increased,² deductions and credits were removed or heavily restricted. The exemption permitted for public pension distributions was severely limited, subjecting retirement income to tax, albeit with a sizable exemption allowance.³ In order to offset the shortfall in revenue owing to the elimination of the MBT, the Governor successfully proposed a 1-percent tax on health care claims made⁴ and took action to renegotiate state employee contracts. Overall, relief to the business community from the Governor's proposal is estimated to be nearly a billion dollars. The overriding intent was to increase Michigan's attractiveness as a place to do business.

The Michigan Corporate Income Tax

The Michigan Corporate Income Tax (CIT) continues many of the attributes of the MBT, while providing several new key provisions that require review and implementation measures before the January 1, 2012, effective date of the tax.

Entities Subject To Tax

Every taxpayer with nexus conducting business activity within

Michigan is subject to the tax. In addition, under the CIT, any person with an ownership interest or beneficial interest in a flow-through entity that has business activity in the state will also be deemed to be subject to tax. The tax is levied at a rate of 6 percent.⁵ The tax is only applicable to C-corporations and unitary business groups. "Corporation" is defined as a taxpayer that has elected or is required to file as a C corporation as defined under sections 1361(a)(2) and 7701(A)(3) of the Internal Revenue Code (the Code).⁶ For the first time since 1976, flow-through entities (partnerships, limited liability companies, and S-corporations) will not be subject to an entity level business tax in Michigan. Instead, the income of flow-through entities is only subject to a single level of tax at the partner or shareholder level. Insurance companies continue to be subject to the gross premiums tax similar to that imposed under the MBT⁷ and financial institutions remain subject to a net capital tax, also similar to that imposed under the MBT.⁸

Interestingly, while the income of flow-through entities may still be included in the tax base of corporate members, the statute does not provide for inclusion of the flow-through entity's factors in the apportionment factor of the corporate member. An open question under the CIT is whether all distributions from flow-through entities are properly includible in the tax base of a corporate member; this is especially the case for distributions related to passive investments or for which there is no flow of value between the flow through entity and its member.⁹

Unitary Business Group and Mandatory Combined Filing Requirement

The CIT continues the imposition of tax on a unitary business group with the mandatory combined filing methodology that came into force with the passage of the MBT.¹⁰ The state's purpose in adopting mandatory unitary business group filing was to prevent the perceived tax planning among members of an affiliated group. Under the CIT, a unitary business group may include corporations (including those partnerships and limited liability companies taxed as corporations) as well as insurance companies and financial institutions. Although insurance companies and financial institutions are not subject to the CIT, inclusion of these entities in the unitary business group ensures that calculation of the unitary business group tax base excludes intercompany transactions. Unitary under the CIT is determined on a water's-edge basis, excluding foreign companies from the unitary group. A unitary business group must be constituted of United States persons. A United States person is defined as "meaning the same as under IRC Section 7701(A)(30)." Foreign operating entities, as specifically defined in the CIT, are not eligible for inclusion in the unitary business group.¹¹

The CIT defines a unitary business group as "a group of U.S. persons, other than a foreign operating entity, one of which owns

or controls more than 50% ownership interest with voting rights or the equivalent of voting rights.”¹² In addition, there must be business activities or operations that create a flow of value or contribution and dependency between or among the corporations in the unitary group. Thus, a unitary business group must meet the control test and one of two alternative relationship tests: (1) the flow of value test, or (2) the integration, dependency, or contribution test. Previously, the Michigan Department of Revenue issued nonbinding Revenue Administrative Bulletins¹³ and frequently asked questions and answers (FAQ)¹⁴ to provide guidance on the application of these tests and the composition of the unitary business group under the MBT. Given the similar statutory definition of a unitary business group, this guidance will likely apply to the unitary business group determinations under the CIT,

Control Test. Under the control test, one member of the unitary business group must own or control more than a 50-percent ownership interest with voting rights or the equivalent of voting rights.¹⁵ In Revenue Administrative Bulletin 2010-1, *Michigan Business Tax Unitary Business Group Control Test*, the Department of Revenue concluded that a person owns or controls more than 50 percent of the ownership interests with voting rights if that person owns or controls, directly or indirectly, (1) more than 50 percent of the total combined voting power of all ownership interests with voting rights or (2) more than 50 percent of the total value of all ownership interests with voting rights. The Department said that an ownership interest with comparable rights to voting rights is one that confers the power to vote in the selection of the management of the entity. In Revenue Administrative Bulletin 2010-1, the Department explained that Parent-Subsidiary and Brother-Sister controlled group of entities will meet the control test where there is more than 50-percent ownership.¹⁶ The Department has also stated that brother-sister entities may constitute a unitary business group, even if the owners are not included in the group.¹⁷ The Department applied section 1563(c) of the Code, except for subparagraph (c)(2) (B), to exclude certain ownership interests from the determination of the control test.

The Department has previously applied rules similar to the federal attribution rules to ownership interests among immediate family members and between corporations and their shareholders to determine control of a unitary business group. Under the Department's interpretation, an individual is deemed to constructively own the ownership interests of his spouse, children, grandchildren, and parents. In addition, a shareholder who owns more than 50 percent in value of the stock of a corporation is considered to own all stock owned directly or indirectly, by or for the corporation in proportion to the value of the stock bears to the value of all the stock of the corporation.¹⁸ Conversely, the corporation is deemed to own all the ownership interests owned, directly or indirectly, by or for that shareholder.¹⁹ The Department has acknowledged that, under the attribution rules, a controlled group of entities may meet the control test but not be under the control of any one member of the group (such as attributed ownership between feuding family members). In such a situation, if the group fails to satisfy the control standards as described by the U.S. Supreme Court, then group is not a unitary business group.²⁰

The Department has also taken the position that a foreign (non-U.S.) entity treated as a single member limited liability company disregarded for federal tax purposes under a U.S. parent company is not includible in a unitary business group.²¹ Accordingly, a foreign SMLLC must file a separate CIT return if the entity has nexus and sufficient business activity in Michigan. The Department has stated that U.S. subsidiaries of a foreign entity may constitute a unitary business group, even though the foreign entity is a separate filer, when both the control and relationship tests are met.²²

Relationship Test. Under the first of the two alternative relationship tests, members are unitary if there is a flow of value between the members. Flow of value has been defined by the Department as created by functional integration, centralized management, and economies of scale.²³ Functional integration is generally demonstrated through common programs or systems and shared information or property.²⁴ Centralized management comes from common management or directors, shared staff functions, and business decisions made for the group, rather than separately by each member.²⁵ Economies of scale include centralized business functions and pooled benefits or insurance.²⁶ Vertically or horizontally integrated businesses, conglomerates, parent companies with wholly owned subsidiaries, and entities in the same general line of business commonly exhibit a flow of value.²⁷ That said, flow of value must be more than the mere flow of funds arising out of passive investment.²⁸

Under the second alternative relationship test, businesses must be integrated with, are dependent upon, or contribute to each other (hereinafter the “integration, dependency, or contribution test”). This test is commonly satisfied when one entity finances the operations of another or when there exist intercompany transactions, including financing.²⁹

Foreign entities with nexus will have to file on a stand-alone basis. Of course, a foreign entity without a permanent establishment in the United States will not have federal taxable income, and the expectation would be that a state corporate income tax would also not apply. Moreover, without a physical presence in the United States, there may be limited federal tax treaty protection for such activities. This may allow the assertion by the Department that the entity must file on a stand-alone basis for CIT filing.

Nexus

Michigan asserts a broad jurisdiction to impose tax under the CIT nexus standard. There are three primary nexus standards under the CIT:

- First, any taxpayer with physical presence within Michigan for more than one day.³⁰
- Second, any taxpayer that actively solicits business in the state and has Michigan sourced gross receipts greater than \$350,000.³¹
- Third, a new standard to Michigan, any taxpayer having an ownership interest or a beneficial interest in a flow-through entity, directly or indirectly through one or more flow-through entities.³²

As a net income tax, the CIT is subject to the limitations of federal Public Law No. 86-272.³³ Under Public Law No. 86-272, a state cannot impose a net income tax if the taxpayer's only contact with the

state is solicitation of orders for sales of tangible personal property when orders are sent outside of Michigan for acceptance and filled by shipment or delivery from outside Michigan. Public Law No. 86-272 protection does not apply to sales of services and intangibles, and if there are any activities other than protected solicitation activities or activities ancillary to solicitation.³⁴

The physical presence standard has been in place under both the SBT and the MBT, and the standards are expected to be same as those under RAB 2008-4, *Michigan Business Tax Nexus Standards*. Nexus creating activities excludes the activities of professionals providing services when those services are not associated with establishing or maintaining the marketplace in Michigan.³⁵

One controversial area of the nexus standard is the imposition of tax on persons whose only activity in the state is “active solicitation” with more than \$350,000 in gross receipts apportioned to Michigan. “Active solicitation” was to be defined in written guidance to be applied prospectively³⁶ that is similar to the standard enacted under the MBT and defined in RAB 2007-6, *Actively Solicits Defined*. A majority of this RAB standard has been codified within the CIT.^{36A} “Actively solicits” is defined as speech, conduct, or activities that explicitly or implicitly invite an order, and activities that neither explicitly or implicitly invite an order but are entirely ancillary to requests for an order. Under the MBT, active solicitation is defined as purposeful solicitation that is directed at or intended to reach persons within Michigan or the Michigan market.³⁷ Purposeful solicitation includes speech or conduct that explicitly or implicitly invites an order or activities that are entirely ancillary to a request for an order. The Department has defined the active solicitation standard to include advertising through print, radio, internet, and television. Under the active solicitation standard, any Michigan businesses is eligible to apportion sales if the business “actively solicits” customers in other states.³⁸ There are 10 other states that assert a statutory economic presence nexus standard. To date, there have been no court decisions on any of these statutory standards.

The newest nexus standard is based upon ownership of an interest in a flow-through entity. Under this standard, an ownership interest in an S-corporation, partnership, or trust will create nexus if the flow-through entity is conducting business activity in Michigan. There is no minimum amount of ownership interest needed to qualify, and although the interest must be a “beneficial” interest, the term is not statutorily defined. An ownership interest can be direct or indirect. Again, the statute lacks clarity and does not define the parameters of what would constitute an indirect interest. Further guidance on this standard will likely be issued by the Department of Revenue, and it is expected that the Department will adopt an attributional nexus standard, concluding that nexus is created due to the attribution of the business activity of the flow-through entity to its corporate members. The Department has stated that if one member of the unitary group has nexus with Michigan, the entire unitary business group has nexus.³⁹ Thus, the flow-through entity can create nexus for the owner’s entire unitary group, even though the flow-through entity itself, by definition, cannot be included within the owner’s unitary business group.

Calculating the Tax Base under the CIT

The CIT base begins with federal taxable income.⁴⁰ The CIT adds back all state, local, and net income taxes deducted in the calculation of federal taxable income, as well as interest and dividend income from other state obligations or securities, less related expenses.⁴¹ In addition, federal net operating loss (NOL) addbacks and carryforwards are eliminated from federal taxable income.⁴² The CIT decouples from IRC Section 168(k) and Section 199, and these amounts are also added back to the CIT base.⁴³ All dividends and royalties from foreign entities and foreign operating entities must also be added back to the extent deducted from federal taxable income.⁴⁴

The CIT continues the MBT related party royalty and interest add-back.⁴⁵ Any deduction for a payment of royalty, interest, or other expense paid to a related person not included in the unitary business group must be added back unless the taxpayer can demonstrate that the transaction has a nontax business purpose, is conducted with arm’s-length pricing and rates and terms as applied in accordance with section 482 and 1274(D) of the federal tax code, and meets one of the following is true: (1) the transaction is a pass-through of another transaction between a third party and the related person; (2) the add-back results in double taxation, (3) the add-back is unreasonable as determined by the Treasurer, or (4) the related party is a foreign person organized in a country with a U.S. tax treaty.⁴⁶ Income and expenses from oil and gas are eliminated from the tax base.⁴⁷

The tax base of a unitary business group is calculated in the same manner except that any intercompany income and expenses are eliminated from the tax base.⁴⁸

Apportionment under the CIT

The CIT continues the single 100-percent sales factor adopted under the MBT. Michigan’s move to a single sales factor was based on the decision to neutralize a business’s decision whether to locate or expand a facility in Michigan. With a single sales factor, a business’s increase in property or payroll in the state will have no effect on its CIT tax burden, inasmuch as there will be no increase in its apportionment factor. Rather, the tax burden is distributed based on the amount of sales made to customers in Michigan. Many of the legislators and others designing the CIT were straightforward in stating that they retained the MBT single sales factor in order to make the new tax as appealing as possible for businesses to locate to, or expand in, Michigan. Thus, all taxpayers who are subject to the CIT will apportion their income based on 100-percent sales factor. The statute specifically provides that a taxpayer may not use the three-factor apportionment provided under the Multistate Tax Compact.⁵⁰

The CIT adopts the *Finnegan* standard of apportionment by statutorily incorporating the rule that the sales of any member of a unitary group is included in numerator of the sales factor, even if that member does not otherwise have nexus in Michigan.⁵¹ The general apportionment rules are destination based or where the customer receives the benefit.⁵² For income from real and personal property, the rules are essentially the same as under the MBT. Income from sales of tangible personal property is sourced to the ultimate destination.⁵³ Income from the sale, lease, rental or licens-

ing, or real property is sourced to the location of the real property.⁵⁴ Rental tangible property receipts are sourced based on the days in state to days everywhere and rental mobile transportation property receipts are sourced based on in-state use.⁵⁵

In general, financial receipts are sourced in accordance with financial apportionment sourcing rules that were previously contained in the MBT and in RAB 2002-14. Royalties and income are sourced to the state where the intangible property was used.⁵⁶ Interest from loans secured by real property is sourced by reference to the location of the real property.⁵⁷ Interest from loans not secured by real property is sourced to the location of the borrower.⁵⁸ Income from sales of services is sourced to where the customer receives the benefit of the services.⁵⁹ If the benefit is received in more than one state, then the receipts are included in the proportion to the in-state benefit.⁶⁰ The MBT alternative apportionment rule that allows taxpayers to petition for use of one or more factors continues.⁶¹ The statute provides that the apportionment provisions are presumed to fairly attribute; in order to obtain permission to utilize an alternative apportionment methodology, therefore, a taxpayer must demonstrate that the business activity attributed to the state is all out of appropriate proportion and leads to grossly distorted result.⁶²

Small Business Credit

The CIT continues the small business credit from the MBT. This "credit" is actually a compliance mechanism that has the effect of phasing in the CIT for up to \$700,000 in gross receipts.⁶³ The small business credit reduces the effective tax rate of qualified small business to 1.8 percent on modified federal taxable income.⁶⁴ Businesses with gross receipts of up to \$20 million will qualify. There are several qualifications in order to take advantage of the small business credit: adjusted business income may not exceed \$1.3 million, and owner/operators cannot receive compensation or distributable shares of income in excess of \$180,000.⁶⁵

Certified Credits

Although vowing to eliminate inducement credits going forward, there were concerns within the Synder Administration about eliminating those credits for which the state had contractually obligated itself to provide, dependent upon the credit recipient satisfying its obligations. These credits are termed "certified credits," since a certificate evidencing the credit would be issued by the Michigan Economic Development Corporation upon completion of the project to which the credit related.⁶⁶ Certified credits include all Michigan Economic Growth Authority (MEGA) Credits (standard, high-tech, rural and retention) that provided a credit based on a percentage of personal income tax withholding over a set period of time; Brownfield Credits; Renaissance Zone Credits for which a development agreement was executed with the Michigan Strategic Fund or part of a collaborative agreement (limiting the Renaissance Zone credit to tool-and-die renaissance zones or Next Energy renaissance zones, not the geographically assigned renaissance zones); Historic Preservation Credits; Michigan Film Credits (both infrastructure and production company credits); Michigan Early Stage Venture Investment Credits; Photovoltaic MBT Cred-

its; Anchor Jobs Credits; Defense Contracting MBT Credits; Anchor District Credits; Polycrystalline Energy Credits; Battery Projection Credits; and Hybrid R&D Technology Credits. Certified credits also include tax vouchers issued by the Michigan Early State Venture Act and specific credits issued for NASCAR activities.⁶⁷

The solution developed by the Administration was to honor the existing certified credits, but only if a taxpayer elects to remain under the MBT regime.⁶⁸ Taxpayers opting to follow the new CIT regime must forgo their certificated credits. The election must be made on the first tax return filed after January 1, 2012, and remains in place for the duration of the certificated credits, including any carryforwards.⁶⁹ One made, the election cannot be changed or amended. If a taxpayer making such election is a member of a unitary business group, the entire group, not just the entity receiving the credit, is required to make the election.⁷⁰

Taxpayers need to carefully calculate their forecasted tax estimates in order to make the correct decision of which alternative is more advantageous. This first-year election is not required for Brownfield Credits or Historic Preservation Credits. For these credits, the taxpayer may choose to elect to file under the MBT in the specific year in which the certificate is received. This exception was permitted only after intense lobbying by developers who rely on the ability to sell the credits to provide funding for the projects, particularly those projects in urban areas. In order to simplify the monetization of these two credits, the statute provides for a refund of these credits at 90 percent of the credit value, which can be requested before the actual filing of the MBT return for the year the credit is claimed.⁷¹ For certain Historic Tax Credits, the refund may be limited to 86 percent.⁷²

The election is also available to flow-through entities and individuals who are no longer subject to an entity level tax under the CIT. Flow-through entities may elect to pay the MBT with offset by a certified credit in lieu of paying the tax due under the IITA.⁷³

The decision whether to make the election is not as straightforward as it first appears. That is because, in determining whether it is more advantageous to stay on the MBT (and offset the tax with credits) or change to the CIT (and forgo any credits), the certified credits are actually applied to the higher of either the MBT liability (including non-certified credits) or the CIT liability. Thus, there can be a haircut against the value of the certificated credit.

To illustrate:

- Step 1:** Determine MBT liability utilizing both non-certified and certified credits and compare to CIT liability with no credits. If the MBT scenario is better, the company would elect to file under the MBT and use their certified credits.
- Step 2:** Once the decision has been made to file under the MBT, the actual certified credit is applied against the higher liability of the MBT liability before the certified credit or the CIT liability.

EXAMPLE	Company A	Company B
STEP 1	MBT Calculation: Calculation: Gross Receipts Liability: \$ 6 mil + Business Income Liability: \$ 3 mil Liability Before Credits: \$ 9 mil - Non-Certified credits \$ 2 mil - Certified credits \$ 5 mil Total Liability \$ 2 mil	CIT MBT Calculation: Calculation: Gross Receipts Liability: \$ 8 mil + Business Income Liability: \$ 2 mil Liability Before Credits: \$10 mil - Non-Certified credits \$ 8 mil - Certified credits \$ 3 mil Total Liability (\$ 1 mil)
STEP 2	MBT Calculation: Calculation: Gross Receipts Liability: \$ 6 mil + Business Income Liability: <u>\$ 3 mil</u> Liability Before Credits: \$ 9 mil - Non-Certified credits <u>\$ 2 mil</u> Liability Before Cert Credits \$ 7 mil - Certified credits \$ 5 mil MTB Liability \$ 2 mil N/A	CIT MBT Calculation: Calculation: Gross Receipts Liability: \$ 8 mil + Business Income Liability: \$ 2 mil Liability Before Credits: \$10 mil - Non-Certified credits <u>\$ 8 mil</u> Liability Before Cert Credits \$ 2 mil - Certified credits \$ 5 mil MTB Liability \$0
Use the Greater Liability		
Summary	Company A Liability = \$2 mil	Company B Liability = \$0

In addition, taxpayers should consider ways to maximize their credits. Opportunities may be available to structure transactions with those entities that currently hold certified credits.

Withholding

As part of the CIT, the withholding provisions for nonresident individuals were maintained and new withholding requirements were passed to require flow-through entities to collect withholding applicable to the CIT on the distributive shares of their members' business income. In order for an entity to be required to withhold CIT, the entity must have more than \$200,000 of business income apportioned to Michigan.⁷⁵ This new withholding regime is in addition to that required under the IITA, which requires withholding under the 4.35-percent personal income tax rate on the distributive share of taxable income of each nonresident member of an entity who is an individual.⁷⁶ A deduction from distributive income is allowed for the proportion of personal and dependency exemptions of the individual allowed under the IITA.⁷⁷

Withholding for corporate members of flow-through entities is at the full statutory rate of 6 percent on the members' distributive share of business income.⁷⁸ For flow-through entity members that are themselves flow-through entities are also subject to the withholding provisions. The statute, however, contains a mechanism to prevent multiple withholding on the same income for tiered partnerships. Under the statute, the Department of Revenue will apply the tax withheld by a flow-through entity on the distributive share of business income of a member flow-through entity to the withholding required of that member flow-through entity.⁷⁹ Additional withholding provisions apply to casinos, race tracks, and eligible film production companies.⁸⁰

This ambiguity in the meaning of "distributive shares" to which the CIT withholding applies raises the potential for the effective withholding rate to exceed the members' actual Michigan liability. In looking to the federal treatment of flow-through entities, a member's distributive share may be affected by offsets (such as suspended losses or other deferred tax attributes) or other provisions of the flow-through entity's operating agreements.⁸¹ In addition, there is the issue how the apportionment factor of the lower-tiered entity is applied in determining the overall Michigan apportionment of the upper-tiered entity. The statute embraces the use of separate accounting methods, which does not align with the adoption of the unitary business group under the CIT. These issues create a likely potential for overwithholding that should be taken into account in preparing CIT quarterly estimates.

Taxes that are withheld will accrue to the state on the last day of the month in which the taxes are withheld, and are required by statute to be remitted within 15 days after the end of the month.⁸² The Department of Revenue has acknowledged that monthly remittance will likely be changed to quarterly for ease of administration.⁸³

Further guidance is anticipated in this area, particularly about whether Michigan will be developing a MI K-1 form for use in reporting. While Michigan does permit composite returns for partnerships, the state has said a composite return for flow-through entities for their corporate members will not be available in 2012.

Transition to the CIT


Similar to the transition from the SBT to the MBT, fiscal-year taxpayers will have a short year for both 2011 and 2012, and the Department is expected to provide transition procedures similar to the MBT. Form development is currently underway, but the new

forms are not expected to be released until after the first of the year. A fiscal-year taxpayer will likely be allowed to file its first return on April 30, 2013, the same as a calendar-year taxpayer, and can elect to calculate income under the annual or actual accounting methods.⁸⁴ Under the annual method, the CIT is calculated for the entire fiscal year and then calculated based on the number of months in the 2012 short year. Under the actual method, taxpayers calculate their tax based upon the actual income and expenses for the month in the 2012 short year.

Estimated tax returns are due on the 15th of April, July, October, and January of each year for calendar-year taxpayers.⁸⁵ Fiscal-year taxpayers must make quarterly estimated tax payments as well.⁸⁶ There is a transition rule for interest and penalties. If a taxpayer pays estimated taxes equal to at least 85 percent of the tax that is otherwise due, then there is no interest and penalty.⁸⁷ The statute appropriates \$1 million for implementation of a new accounting system and a new computer system to be able to accept electronic returns. The million-dollar appropriation ensures that this tax bill cannot be repealed by a referendum, as under Michigan law, bills that appropriate money are not subject to referendum and petition drives.

Summary

Taxpayers should give thoughtful consideration of the effect of the change to the CIT. Year-end planning should include analysis of the benefits to be gained from the acceleration of deductions into 2011, as well as the deferral of gain until 2012. In addition, fourth-quarter transactions should be viewed with an eye toward maximizing any MBT net operating losses or carryforwards that will disappear as of January 1, 2012.

One thing is certain, the tax landscape continues to change in Michigan and taxpayers must stay alert for proposed guidance, rules, and case law that will further define the new Michigan corporate income tax. 

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1. Michigan Government's fiscal year begins October 1.
2. The current rate of 4.35 percent was scheduled to drop to 4.25 percent in 2012; this reduction was delayed one year and is now scheduled to occur on January 1, 2013.
3. Previously, federal and public pension distributions enjoyed tax-exempt status and private pensions were exempt up to \$42,240 for a single return and \$84,480 for a joint return. MCL 206.30(1)(f).
4. 2011 PA 141 and 142..
5. MCL 206.623.
6. MCL 206.605(1).
7. MCL 206.635.
8. MCL 206.653. There were also minor changes to the net worth tax for treasury balances.
9. The Supreme Court of the United States has held that, under the Commerce Clause, a state cannot constitutionally tax income that does not arise from unitary business conducted in the state (*Allied Signal, Inc. v. Division of Taxation*, 504 U.S. 768 (1992)) and that the income from a unitary business group must be fairly apportioned (*Complete Auto Transit, Inc. v. Brady*, 430 U.S. 976 (1977)).
10. MCL 206.611(5); 206.691.
11. MCL 206.607(3) defines a foreign operating entity as a U.S. person that has substantial operations outside the United States, the District of Columbia, any territory or possession of the US except the commonwealth of Puerto Rico and at least 80 percent of its income is active foreign business income as defined in section 861 (C)(1)(b) of the Code. Under the federal tax law, businesses operating and generating income in a U.S. possessions or territory generate foreign source income. So it seems illogical, and also contrary to other states' definitions of 80/20 companies, that the Michigan foreign operating entity definition requires substantial operations outside U.S. possessions and Puerto Rico along with 80 percent of its income as active foreign business income, which could include income from Puerto Rico and the U.S. possessions and territories.
12. MCL 206.611(6).
13. RAB 2010-1 *Unitary Business Group Control Test* and RAB 2010-2 *Unitary Business Group Relationship Test*. Revenue Administrative Bulletins (RABs) are not issued in accordance with the Michigan Administrative Procedures Act, 1969 PA 306, and thus do not have the force and effect of law. Although RABs are not binding on taxpayers or the state, the Department of Revenue has issued an RAB claiming to be bound by the positions in its Revenue Administrative Bulletins. RAB 89-39.
14. See <http://www.michigan.gov/taxes/0,1607,7-238-47449---F,00.html>.
15. MCL 206.611(6).
16. RAB 2010-1, III(B), Example 6.
17. See FAQ 34 and 39.
18. RAB 2010-1, VII.
19. *Id.*
20. RAB 2010-1, III (E).
21. See FAQ 31 and 36.

22. FAQ 36.
23. Revenue Administrative Bulletin 2010-2, *Michigan Business Tax Unitary Business Group Relationship Tests* (RAB 2010-2).
24. *Id.*
25. *Id.*
26. *Id.*
27. *Id.*
28. *Id.*
29. *Id.*
30. MCL 206.621(1).
31. *Id.*
32. *Id.*
33. 15 U.S.C. §§ 381 to 384.
34. A list of unprotected activities is specified in subsection II.C. of RAB 2008-4, *Michigan Business Tax Nexus Standards*.
35. MCL 206.621(3).
36. MCL 206.621(2).
- 36a. Enrolled Senate Bill 669, P.A. 183 of 2011, effective October 18, 2011.
37. Revenue Administrative Bulletin 2007-6, *Actively Solicits Defined*.
38. MCL 208.621 provides that a taxpayer may apportion if another state would have jurisdiction to impose a tax of the type provided under the CIT.
39. FAQ N12; RAB 2008-4.
40. MCL 206.603(2).
41. MCL 206.603(2)(b).
42. MCL 206.603(2)(c).
43. MCL 206.603(2)(d).
44. MCL 206.603(2)(a).
45. MCL 206.603(2)(e).
46. *Id.*
47. MCL 206.603(2)(f).
48. MCL 206.691.
49. MCL 206.661(2).
50. MCL 206.663(3). The statutory prohibition against using the MTC three-factor formula is effective prospectively from January 1, 2011, implying a permissive use of the factor for periods before 2011. Taxpayers should consider possible claims for periods still open.
51. MCL 206.663(2).
52. MCL 206.665.
53. MCL 206.665(1)(a).
54. MCL 206.665(1)(b).
55. MCL 206.665(1)(c), (d).
56. MCL 206.665(1)(e).
57. MCL 206.665(4).
58. MCL 206.665(5).
59. MCL 206.665(2)(c).
60. *Id.*
61. MCL 206.667.
62. MCL 206.667(3).
63. MCL 206.671.
64. MCL 206.671(4).
65. *Id.*
66. The certificate is technically issued by the Department of Treasury upon the submission of a Request for Certificate of Completion that is submitted by the taxpayer upon the completion of the project, or a particular project phase, depending if the project is a phased project.
67. MCL 208.107.
68. MCL 206.608(1). This is why the MBT was not repealed with the enactment of the CIT. Such repeal will not occur until the Secretary of State receives a written notice from the Department of Treasury that the last certified credit or any carryforward from that credit has been claimed. See Enacting Section 1, 39 PA 2011.
69. MCL 206.608(2).
70. MCL 208.500(1).
71. MCL 206.510.
72. MCL 206.510(2).
73. MCL 206.500(2).
74. MCL 206.703.
75. MCL 206.703(2).
76. MCL 206.703(3). The rules for withholding by pass-through entities for income tax of individual nonresident owners were enacted effective October 1, 2003, and have not changed; withholding of personal income tax is still required.
77. *Id.*
78. "Business income" has the same definition as contained in MCL 206.603(2).
79. MCL 206.703(5).
80. MCL 206.703(5) *et seq.*
81. The most common items include guaranteed payments, redemption of partnership interests, cash distributed in excess of partnership basis and crediting of distributions.
82. MCL 206.703(10).
83. The Department has the authority to require remittance at other times than monthly, if the Department has reasonable grounds to believe that a flow-through entity will not pay taxes withheld to the state. MCL 206.705. In addition, an annual reconciliation return is required under MCL 206.771, and the state may require an annual business income information return under the same provision.
84. MCL 206.683 (A) and (B).
85. MCL 206.681(2).
86. *Id.*
87. MCL 206.681(3).