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Treasury Clarifies Unitary Business Group Issues for the Michigan Business Tax

GRAND RAPIDS, MI – Monday, January 28, 2008 – The Michigan Department of Treasury (Treasury) issued a series of Frequently Asked Questions (FAQs) this month that addressed several issues with the Michigan Business Tax (MBT) including the "unitary business group" and the "combined" filing requirement for a "unitary business group". Following is a discussion of "unitary business group" issues.

Two FAQs tried to reconcile the apparent conflict between Section 117(5) which states a "Taxpayer means a person or a unitary business group..." and Section 511 which states "Each ... person included in a unitary business group ... shall be treated as a single person ..."

A taxpayer under the MBT includes a unitary business group. MCL 208.1117 (5).

A unitary business group is comprised of two or more U.S. persons. MCL 208.1117(6).

Nexus exists if the taxpayer has (1) physical presence in Michigan for more than one day during the tax year or (2) actively solicits sales in Michigan and has gross receipts sourced to Michigan of \$350,000.00 or more. MCL 208.1200.

Thus, a taxpayer that is a unitary business group has nexus with Michigan so long as any one member of the unitary business group has nexus with Michigan. The taxpayer that is a unitary group is required to file a combined return under MCL 208.1511. (Treasury FAQ U-12)

The requirement to include in a "unitary business group", entities that do not have nexus with Michigan and to include the Michigan sales of such entities in the numerator of the apportionment formula sales factor is provided for in Section 303(2).

Except as otherwise provided under this subsection, for a taxpayer that is a unitary business group, sales include sales in this state of every person included in the unitary business group without regard to whether the person has nexus in this state. Sales between persons included in a unitary business group must be eliminated in calculating the sales factor. MCL 208.1303(2)

The basic premise in filing a combined/unitary return is that all activities carried on by separate entities are part of a single unitary business, one taxpayer. Under the "Finnigan" concept, a taxpayer is defined to mean all members of a unitary group. The combination of Michigan Business Tax Act (MBTA) Section 117(5) and Section 303(2) both cited above provide legislative authorization for Michigan to adopt the Finnigan concept. *California State Board of Equalization in the Appeal of Finnigan Corporation (Finnigan), Cal. St. Board of Equal., Jan 24, 1990 (88-SBE-022A)*

This "Finnigan" concept only applies to entities who file a unitary/combined tax return in Michigan

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and does not apply to entities not filing combined returns in Michigan.

Under "Finnigan" and MBTA Section 303(2), sales made by a member of the unitary group to a destination in Michigan would be included in the numerator of the sales apportionment factor even if the member did not have nexus with Michigan. There is no "throwout" of the Michigan destination sales because the member did not have nexus with Michigan. Michigan does not have a "throwback" rule which means sales from Michigan to a state where the taxpayer is not taxable are **not** thrown back to Michigan and included in Michigan sales.

Section 511, which states "Each ... person included in a unitary business group ... shall be treated as a single person ...", appears to be in conflict with the above discussion and Section 117(5). Treasury reconciles the two sections as follows:

The phrase "shall be treated as a single person" in section 511 of the MBTA, MCL 208.1511, relates to the removal of transactions between unitary business group members from the determination of the business income tax base, the modified gross receipts tax base and the apportionment formula of a unitary business group as a distinct taxpayer.

Phase-ins, thresholds, credit limits and other components to determining tax liability relate to the unitary business group as a distinct taxpayer, not to the individual persons that comprise the unitary business group. The unitary business group, to which individual "persons" might belong, is treated as the taxpayer -- a distinct entity -- for purposes of tax liability under the MBTA.

Although a person can be a taxpayer under the MBTA, a person that is a member of a unitary business group is not the taxpayer, rather the unitary business group to which that person belongs is the taxpayer.

Accordingly, the phrase in MCL 208.1511 does not cause the individual members of a unitary business group to be treated as separate, individual taxpayers for purposes of determining tax liability under the MBTA. (Treasury FAQ U-14)

Treasury has provided guidance on how a combined return will be prepared when members of the unitary business group have different methods of accounting and different year ends.

The Michigan Business Tax Act does not require each member of a unitary business group to use the same method of accounting to determine its business income.

A taxpayer that is a unitary business group must file a combined return under MCL 208.1511 using the tax year of the designated member. On the combined return, the business income of each member should reflect the accounting method the member used to compute its federal taxable income, whether cash or accrual.

"Designated member" means a member of a unitary business group that has nexus with Michigan under MCL 208.1200 and that will file the combined return required under section 511. If the member that owns or controls the other members of the unitary business group has nexus with Michigan, then that controlling member must be the designated member.

The combined return of the unitary business group must include each tax year of each member whose tax year ends with or within the tax year of the designated member.

The business income of a unitary business group is the sum of the business income of each person included in the unitary business group, other than a foreign operating entity or a person subject to the tax on insurance companies or financial institutions, less any items of income and related

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deductions arising from transactions, including dividends, between persons included in the unitary business group. MCL 208.1201(4). (Treasury FAQ U-17)

Please stay tuned for more news and follow the [MichiganStateAndLocalTax Blog](#) for information as it becomes available.

If you have questions please feel free to contact me. I would be happy to be of assistance.

Sincerely,

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