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**STATE AND LOCAL TAX NEWSLETTER**

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**Treasury Clarifies MBT Issues with Individuals, Estates, Trusts,  
Family Limited Partnerships and Investment Partnerships**

**GRAND RAPIDS, MI - Monday, February 25, 2008 -** Since the passage of the Michigan Business Tax (MBT), there has been a lot of confusion as to what extent individuals, estates, trusts, family limited partnerships, and investment partnerships would be subject to the MBT.

The MBT definition of "person", "taxpayer", and "business activity" would subject individuals, estates, trusts, family limited partnerships and investment partnerships to the MBT. The MBT is much more than just a "business" tax.

**Definition of Person**

The definition of "person" includes an individual, limited partnership, receiver, estate, trust or any other group or combination of groups acting as a unit. The definition is all encompassing and designed to include individual and entities not normally associated with a trade or business or business activity. More importantly, such entities could and may be drawn into a "unitary business group".

**(3) "Person" means an individual, firm, bank, financial institution, insurance company, limited partnership, limited liability partnership, co-partnership, partnership, joint venture, association, corporation, subchapter S corporation, limited liability company, receiver, estate, trust, or any other group or combination of groups acting as a unit. [MCL 208.1113(3)]**

**Definition of Taxpayer**

The definition of taxpayer contained in Section 117(5) [MCL 208.1117(5)] includes a "person" as defined above. It also includes a "unitary business group". When the two definitions are put together, it could involve the inclusion of an individual or individuals, not normally subject to the MBT,

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into a "unitary business group" and make them a taxpayer.

To the extent that a limited liability company is a single member limited liability company disregarded for federal tax purposes, then the owner of that limited liability company will be the taxpayer under the MBT. The disregarded single member limited liability company will be treated as a sole proprietorship, branch, or division of its owner. [Treasury FAQ Mi5]

### **Definition of Business Activity**

The definition of "business activity" by the absence of specific exclusions includes casual sales, isolated sales, investment activities and non-business income.

**(1) "Business activity" means a transfer of legal or equitable title to or rental of property, whether real, personal, or mixed, tangible or intangible, or the performance of services, or a combination thereof, made or engaged in, or caused to be made or engaged in, whether in intrastate, interstate, or foreign commerce, with the object of gain, benefit, or advantage, whether direct or indirect, to the taxpayer or to others, but does not include the services rendered by an employee to his or her employer or services as a director of a corporation. Although an activity of a taxpayer may be incidental to another or to other of his or her business activities, each activity shall be considered to be business engaged in within the meaning of this act.**

**[MCL 208.1105(1)]**

There is no exclusion from the definition of "business activity" for casual sales as contained in the Single Business Tax Act. [MCL 208.4(1)]

Therefore, transactions made or engaged in other than in the ordinary course of repeated and successive transactions of a like character, which are exempt from the SBT, are included as a "business activity" subject to the MBT.

There is no exclusion from the definition of "business activity" for an isolated sale as contained in the Sales Tax Act. "Business activity" includes an activity that may be incidental to another person or to other of his or her business activities.

There is no exclusion from the definition of "business activity" for non business income as contained in many other state tax laws. Although the MBT is a tax imposed on "business activity", in fact, it is imposed on non business income derived from outside of the regular course of business of the taxpayer.

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There is no exclusion from the definition of "business activity" for investing activities. Therefore, dividend, interest or royalty income and capital gains are included in "business activity" and subject to the MBT unless the "organized exclusively for estate and gift planning purposes" exclusion is applicable.

**Public Act 245 of 2007**

The legislature in PA 145 of 2007 provided a minor exclusion for an individual, estate, partnership organized exclusively for estate or gift planning purposes, or a trust organized exclusively for estate or gift planning purposes. Treasury has recently provided some explanation of both the amendments and how they fit into the MBT.

**Treasury Clarification**

The Treasury responded in FAQ B8 to whether the business income tax and modified gross receipts tax components of the MBT apply to individuals, estates, and trusts or family limited partnerships (FLIP)s that are specifically established for estate planning purposes.

**No. The definitions of "business income" and "gross receipts" as used in the MBT act were amended on December 1, 2007 by P.A. 145 to specifically exclude this type of income received by these types of entities from the MBT tax bases and threshold amounts.**

**Personal investment income, gains from the sale of personal assets or other assets not used in a trade or business, and any other income not specifically derived from a trade or business that is earned, received, or otherwise acquired by an individual, an estate, or a trust or partnership organized or established exclusively for estate or gift planning purposes, are not included in gross receipts for purposes of determining the filing thresholds under sections 200, 411, or 505 (MCL 208.1200, 208.1411, or 208.1505), and are not included in the business income tax base or modified gross receipts tax base under sections 201 and 203, respectively, (MCL 208.1201 and 1203).**

**This exclusion only applies to the specific types of entities identified above. Investment income and any other types of income earned or received by all other types of persons or entities not specifically referenced in these revised definitions must be included in the gross receipts and business income of the taxpayer. [Treasury FAQ B8]**

In Treasury FAQ Ap4, the apportionment issues relating to an investment partnership were addressed. Is it based on the residence of the general

partner, the location of the brokerage firm, the residences of the majority of partners, or where the partnership was formed?

**An investment partnership is typically organized as a limited partnership in which the investors (or limited partners) pool funds that are professionally managed by a money manager who acts as a general partner. The money manager generally has a small ownership interest in the partnership and is compensated through a set management fee and a designated percentage of the overall partnership investment profits.**

**For purposes of the MBT, a taxpayer is subject to tax in Michigan if the taxpayer has (1) substantial nexus in Michigan as defined in section 200 (MCL 208.1200) and (2) meets the gross receipts threshold of \$350,000 under section 505 (MCL 208.1505). Substantial nexus is defined to mean either a physical presence in this state for a period of more than 1 day during the tax year or engagement in active solicitation of sales in this state with Michigan sourced gross receipts of \$350,000 or more.**

**In the typical investment partnership described above, the location of the office from which the fund manager or general partner conducts the business activity of the partnership would constitute physical presence for purposes of the MBT nexus standards under MCL 208.1200. If this office is located in Michigan, the partnership would have physical presence in Michigan and have nexus for purposes of the MBT. If the gross receipts of this partnership were \$350,000 or more, the partnership would be subject to MBT. [Treasury FAQ Ap4]**

Passage of the PA 145 provisions relating to an individual, estate, partnership organized exclusively for estate or gift planning purposes, or a trust organized exclusively for estate or gift planning purposes was designed to stop the flow of capital out of Michigan in order to avoid the MBT. PA 145 was very narrowly drafted and the phrase "exclusively for estate or gift planning purposes" is troublesome. Most trusts could fit into the "exclusively for estate or gift planning purposes" category. However, most family limited partnerships and investment partnerships would not fit the "exclusively" exclusion language.

Many family limited partnerships and investment partnership are considering a move out of Michigan to avoid the MBT. In FAQ Ap4, the Department of Treasury narrowly identified the type of activity that would create nexus in Michigan. Assuming the assets in the family limited partnership and investment partnership are passive in nature, nexus in

Michigan and the MBT could be avoided if "the location of the office from which the fund manager or general partner conducts the business activity of the partnership" was not in Michigan. If the office, referenced in FAQ Ap4, is **not** located in Michigan, the partnership would **not** have a physical presence in Michigan and **not** have nexus for purposes of the MBT.

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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