

INTERNAL POLICY DIRECTIVE 2006-4

August 15, 2006

SINGLE BUSINESS TAX Non-corporate Entity Casual Transaction

INTRODUCTION

This Internal Policy Directive (IPD) is intended to provide guidance to departmental personnel on the issue of casual transactions for noncorporate entities. Corporations do not qualify for a casual transaction under the Single Business Tax Act. The IPD provides examples of transactions that may qualify or not qualify as a casual transaction. These examples are not exhaustive but are illustrative of different types of transactions.

POLICY ISSUES

- A. The Department has identified the sale of an individual's personal residence as qualifying as a casual transaction. Are there other transactions by an individual that the Department will consider a casual transaction?
- B. How is the phrase "repeated and successive transactions of a like character" interpreted?
- C. How is the phrase "incidental to that person's regular business activity" interpreted?

POLICY DETERMINATION

- A. Yes. The Department will presume that sales of intangible investment assets by an individual that are not incidental to the individual's regular business activity, and that result in gross receipts of less than \$350,000 in any one tax year, are not "repeated and successive," and are casual transactions.
- B. The decision of whether a transaction is deemed to be a repeated and successive transaction of a like character to other transactions will be determined on a case by case analysis.
- C. A transaction will be deemed incidental to a person's regular business activity if the transaction happens as a result of or in connection with a regular business activity that is more important; if the transaction is subordinate to a regular business activity of greater value or; the transaction has a minor role in the regular business activity.

DISCUSSION

A transaction that occurs either in the ordinary course of repeated and successive transactions of a like character or that is incidental to a person's regular business activity does not qualify as a casual transaction.

A. Notwithstanding the discussion under Part B below, the Department will presume sales of intangible investment assets by an individual that are not incidental to the individual's regular business activity, and that result in gross receipts under \$350,000 in any one tax year, are not "repeated and successive," and are casual transactions. If the gross receipts equal or exceed \$350,000 in any one tax year the presumption does not apply and all the facts and circumstances will be evaluated to determine if the transaction is "repeated and successive."

B. A transaction that occurs in the ordinary course of repeated and successive transactions of a like character does not qualify as a casual transaction. Casual transaction is defined as:

(1) "Casual transaction" means a transaction made or engaged in other than in the ordinary course of repeated and successive transactions of a like character, except that a transaction made or engaged in by a person that is incidental to that person's regular business activity is a business activity within the meaning of this act.¹

Neither the SBTA nor the federal income tax code defines the terms "repeated" or "successive." Therefore the Department will rely on the common understanding of those terms. Webster's New World Dictionary (Third College Edition) defines "repeated" as "happening again." In addition, it defines "successive," to mean "following in uninterrupted course; consecutive."

Accordingly, a transaction that is performed once will not be considered "repeated." This does not mean, however, that a transaction will necessarily be deemed repeated if it occurs more than once. The frequency of the transaction or like transactions will be determined and evaluated on a case by case basis. A transaction will be deemed repeated if other transactions of a like character have occurred during the taxpayer's existence.

A transaction that is performed once will not be considered "successive" as it is not consecutive. To determine if a transaction is successive the business activity of the taxpayer must be evaluated. If the transaction occurs in a manner that can be considered consecutive or occurs in an uninterrupted course it will be deemed successive. Business practices of the taxpayer may be used to determine if the transaction is "successive." Again, the transaction can be deemed successive if more than one transaction of a like character has occurred during the taxpayer's existence.

With regard to the terms "repeated" and "successive," a one-time transaction is the best example of a transaction that is not "repeated and successive." As transactions of a like character increase in frequency, the more likely it is that the transaction will be considered repeated and successive. The determination will be based on all the facts and circumstances surrounding the person's business activity and the nature of the transaction. It is important to note that either of these criteria - repeated and successive, or incidental to a person's regular business activity - will disqualify a transaction from casual status. The concept of incidental is addressed below.

C. A transaction that is not "repeated and successive" nevertheless will not qualify as a casual transaction if it is incidental to the person's regular business activity. Again, the terms "regular" and "incidental" are not defined in the SBTA or the federal income tax laws. Accordingly, the use of common understanding of the terms is appropriate.

¹ MCL208.4(1)

Webster's New World Dictionary (Third College Edition) defines "regular" in pertinent part as, "[c]ustomary, usual, or normal." A transaction will not qualify as a casual transaction if it is incidental to the customary, usual, or normal business activity of the person engaging in the transaction.

Incidental means as a result of or in connection with something more important; subordinate to something of greater value; having a minor role, etc. See Webster's New World Dictionary (Third College Edition) and Black's Law Dictionary (Eighth Edition).

Accordingly, if a transaction occurs as a result of or in connection with something more important or is subordinate to the person's usual business activity, the transaction will be considered incidental to the person's regular business activity. As such, the transaction would not qualify as a casual transaction.

EXAMPLES

1. A retailer finalizes the sale of one widget during the tax year. It is the only widget he has ever sold, but he finalizes thousands of sales of other types of merchandise. The retailer is engaging in a transaction (selling a widget) of a like character to other transactions (selling other types of merchandise) that has occurred more than once and is uninterrupted and consecutive. The sale of the widget is not a casual transaction.
2. Joe has a personal investment portfolio of stocks that he manages throughout the year. Joe does not engage in the sale or trading of any other personal assets or negotiable instruments and has no other business activity. Joe's gross receipts from the sale of stock equal \$300,000. The Department will presume that an individual's sales of their intangible investments are not repeated and successive transactions, and therefore are casual transactions, as long as the sales produce gross receipts of less than \$350,000 in the taxable year. If the sales exceed \$350,000, the Department will look at all the facts and circumstances, including but not limited to, the number of sales and the period of time over which the sales occurred, in order to determine if the transactions are "repeated and successive."
3. Joe has a personal investment portfolio of stocks that he manages throughout the year. Joe also owns and operates a restaurant as a sole proprietor. Joe has gross receipts of \$300,000 from the sale of stock. Joe also has gross receipts of \$400,000 attributable to the operation of his restaurant. The Department will presume that Joe's sale of personal intangible investments are not repeated and successive transactions, and therefore are casual transactions. However, Joe has a filing responsibility for the \$400,000 attributable to the operation of his restaurant.
4. Company A engages in the business activity of making car bumpers. After several years of operation, Company A sells a metal press. The sale of the metal press is incidental to Company A's regular business activity of manufacturing car bumpers. A subordinate or a minor role in operating a business is the periodic sale of assets. Accordingly, the sale of the press is not a casual transaction.
5. Partnership A owns an interest in multiple partnerships, including Partnership B. Partnership A decides to sell its interest in Partnership B to an outside party. The sale would not be a casual transaction because the sale would be incidental to Partnership A's regular business activity.

Because "S corporation" is defined as a corporation under the Internal Revenue Code, an S corporation may not have a casual transaction for purposes of computing SBT liability. Therefore, an S corporation that sells an interest in a partnership shall not claim the transaction is a casual transaction.

CONCLUSION

A transaction that is engaged in other than during the ordinary course of repeated and successive transactions of a like character, and that is not incidental to the person's regular business activity, qualifies as a casual transaction. All relevant facts and circumstances should be considered in determining whether a transaction is repeated and successive. If the sales of intangible investments by an individual are not incidental to the individual's regular business activity, and result in gross receipts of less than \$350,000 in the taxable year, the transactions will be presumed not to be "repeated and successive," and to be casual transactions.