



STATE OF MICHIGAN
DEPARTMENT OF TREASURY
LANSING

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**NOTICE TO TAXPAYERS REGARDING
*LABELLE MANAGEMENT INC v DEPARTMENT OF TREASURY***

Issued: February 28, 2017

I. Summary of *LaBelle Management Inc v Department of Treasury*

On March 31, 2016, the Michigan Court of Appeals issued a decision in *LaBelle Management Inc v Department of Treasury* (“*LaBelle*”).¹ At issue in *LaBelle* was the meaning of indirect ownership as used in the unitary business group (“UBG”) definition under section 117(6) of the Michigan Business Tax Act (“MBTA”).²

A UBG is a group of related United States persons, other than a foreign operating entity, whose business activities or operations are interdependent. Specifically, it is two or more persons that satisfy both a control test and one of two relationship tests. The control test is satisfied when one person owns or controls, directly *or indirectly*, more than 50% of the ownership interest with voting or comparable rights of the other person or persons.³ *LaBelle Management* challenged the Department’s interpretation of the control test, as set forth in Revenue Administrative Bulletin (“RAB”) 2010-1. Specifically, *LaBelle* challenged the Department’s reliance upon IRC 318 to define indirect ownership to include constructive ownership, or ownership through attribution.

Reversing the Court of Claims, the Court of Appeals found in favor of *LaBelle Management*, holding that indirect ownership as used in the MBT definition of a UBG means ownership “through an intermediary.” However, the Court of Appeals subsequently issued an order staying the effect of its decision until the Department’s appeal rights were exhausted. On January 24, 2017, the Supreme Court denied the Department’s Application for Leave to Appeal. The Stay of the Court of Appeals decision is now lifted.

II. Impact of Denial of Leave in *LaBelle Management Inc v Department of Treasury*

The Supreme Court’s denial of the Department’s Application for Leave to Appeal and the removal of the Stay makes the Court of Appeals decision binding precedent. The Department

¹ 315 Mich App 23 (2016).

² MCL 208.1117(6).

³ MCL 208.1117(6).

will give the Court of Appeals decision full retroactive effect and will apply it to all open tax years.⁴

The Court of Appeals decision eliminates constructive ownership or ownership through attribution as a means of satisfying the UBG control test. Since the same control test is used for both the MBT and the Corporate Income Tax (CIT), the Department views the *LaBelle* decision as applicable to both taxes. The Department interprets the Court's decision as narrowing UBG groups to those in which ownership or control is based upon a parent-subsidary chain of relationships. For example, where Corporation A owns 51% of Corporation B, which owns 51% of Corporation C, which owns 51% of Corporation D, all 4 Corporations form a parent-subsidary controlled group under *LaBelle* because Corporations B and C are both permissible intermediaries through which Corporation A indirectly controls both Corporations C and D as well as directly controlling Corporation B.

UBGs with members whose membership is based upon a brother-sister relationship as described in RAB 2010-1 do not meet the requisite level of control under *LaBelle*. Nor do mere custodial or possessory interests rise to the requisite level of ownership or control necessary to satisfy Section 117(6) of the MBT Act.⁵ In that regard, the following sections of RAB 2010-1 and RAB 2013-1 are rescinded: Section III(B), (C), and (E), Section VI, and Section VII. Consequently, UBGs and members affected by the *LaBelle* decision must correct their filings for all open years to conform to the decision.

To the extent that the designated member of an affected UBG remains the designated member of a UBG that no longer contains all of its previous members after applying *LaBelle*, the designated member must file amended returns for all open years, including on the returns only those members that meet the control test under *LaBelle*.

Those members who do not meet the control test under *LaBelle* must determine whether they meet the control test for inclusion in a separate UBG or whether they are a stand-alone filer for the open years. In either case, the affected member of the former UBG is considered a non-filer for the years that it filed in conformance with the Department's guidance in RAB 2010-1 or RAB 2013-1. Affected entities must file returns for those years either as a single taxpayer or as a member of the new UBG under the new UBG's designated member. However, the Department will require these entities to file amended returns, or original returns for new stand-alone filers, only for those tax periods within the limitations period prescribed by MCL 205.27a(2),⁶ and the Department will not assess these entities as non-filers for tax periods prior to that period.

⁴ The Department is required to give judicial decisions full retroactive effect – even in the presence of contrary guidance issued by the Department prior to the date of the decision. See *Syntex Laboratories v Dep't of Treasury*, 233 Mich App 286 (1998); *Rayovac Corp v Dep't of Treasury*, 264 Mich App 441 (2004); *JW Hobbs v Dep't of Treasury*, 268 Mich App 38 (2005); *Int'l Home Foods Inc v Dep't of Treasury*, 477 Mich 983 (2007).

⁵ The Department interprets the Court's reference to definitions in *Black's Law Dictionary* and *Fletcher's Cyclopaedia* as emphasizing the importance of an intermediary in establishing indirect ownership or control and not as its approval of possessory or custodial arrangements as sufficient to establish ownership or control.

⁶ See LR 2015-2, (http://www.michigan.gov/documents/treasury/LR_2015-2_-_Administration_of_PA_3_491518_7.pdf). Whether a period is open under the statute of limitations may depend on whether an audit commenced, 2014 PA 3.

Penalties will not be imposed for amended UBG returns or original stand-alone returns that are a direct result of *LaBelle*.

All returns filed as a result of *LaBelle*, whether amended or original, should be accompanied by written correspondence identifying the return as a “*LaBelle*” return. Any entity entitled to a refund as a result of compliance with *LaBelle* may direct the Department to transfer the overpayment to the accounts of other members of the former group that are now filing separately if the member entity entitled to the refund and the member entities to whom the transfer is to be made file returns simultaneously (that is, if the returns are mailed together).

If the return is an amended return filed by the designated member of the newly configured UBG and the return reflects an overpayment, the DM must attach written correspondence specifying the date the payment was made, the amount of the payment, and the manner in which the overpayment should be allocated among former or current members of the UBG if the DM was the entity who made the prior overpayment on behalf of its members. If no payment transfer is requested, any overpayment will be refunded or credited to the account of the DM, and it will be up to the members of the former group to allocate these funds.

In the event that a member entity other than the DM made a payment and that member is affected by the *LaBelle* decision and ceases to be a member of the former UBG, the entity’s payment will automatically move to its own account unless the entity instructs the Department otherwise. Written correspondence directing the application of a payment made by a former member/entity must specify the date the payment was made, the amount of the payment, and the manner in which the overpayment is to be allocated.

DMs authorized by their member entities to act on behalf of the UBG will continue to have the authority to discuss and receive information related to any return it filed on behalf of the UBG prior to the *LaBelle* decision. To the extent that the composition of the UBG is affected by the *LaBelle* decision, the affected entities should ensure that the appropriate form delegating the authority to act on their behalf is executed and submitted to the Department.

III. Interest Waivers

The Department will waive interest for amended UBG returns or original stand-alone returns that are a direct result of *LaBelle* so long as those returns are filed by December 31, 2017.