Flow-Through Entity Annual Return (Form 5772) Instructions 2022

Purpose

To calculate and report the annual Flow-Through Entity tax (FTE tax) under Part 4 of the Michigan Income Tax Act, for a flow-through entity (FTE) that has made an election to file and pay the tax.

Common Terms Used In these Instructions

Member when used in reference to a flow-through entity, means a shareholder of an S corporation or a partner or member in a partnership. A member can be an individual, trust, or estate, regardless of residency in Michigan, another flow-through entity, or a C corporation, insurance company, or financial institution under the CIT. However, income or loss attributed to a member that is a C corporation, insurance company, financial institution is not subject to the FTE tax.

Tax year means the calendar year, or the fiscal year ending during the calendar year, upon the basis of which the tax base of a taxpayer is computed under Part 4 of the Income Tax Act. If a return is made for a fractional part of a year, tax year means the period for which the return is made. A taxpayer that has a 52- or 53-week tax year beginning not more than 7 days before the end of any month is considered to have a tax year beginning on the first day of the subsequent month.

A member's tax year that ends with or within the taxpayer's tax year is referred to in these instructions as *the same tax year*. For example, Company X has two individual owners, Y and Z. Company X's tax year ends June 30, 2022. Y and Z's tax years end December 31, 2022. If X is the filer of this return, its tax year ending in 2022 is reported on this 2021 form. Y and Z file their individual income tax (IIT) returns on 2022 forms. However, these instructions will refer to Y and Z's 2022 tax year as the same tax year as Company X's ending June 30, 2022.

Who Should File?

Flow-through entities that have nexus with Michigan and that have made an election for a tax year that begins in 2022 must file this annual return.

For purposes of this tax, *flow-through entity* means an entity that for the applicable tax year is treated as an S corporation or a partnership under the internal revenue code for federal income tax purposes. Flow-through entity does not include a publicly traded partnership, a disregarded entity, or a financial institution subject to the Corporate Income Tax (CIT) franchise tax.

Taxpayer as used in these instructions refers to a flow-through entity that has nexus in Michigan and elects to be subject to the flow-through entity tax under Part 4 of the Michigan income tax act.

Election into the Tax. An election to pay the flow-through entity tax must be made by the fifteenth day of the third month of the flow-through entity's tax year (March 15 for calendar year filers). The election is effective for the tax year in which the election is made and for the next two successive tax years (3 years total). Once made, the election is irrevocable. .

The election can be made only by submitting an electronic payment to the Department through Michigan Treasury Online (MTO). To be valid, the payment must be designated as applicable to the tax year for which the election becomes effective. There is no requirement as to the amount of the payment. For example, the payment could be made in a nominal amount, or it could be equal to the flow-through entity's first quarter estimated payment. Payments submitted outside of MTO will not constitute a valid election to pay the flow-through entity tax.

Nexus. A taxpayer is subject to the flow-through entity tax if the taxpayer makes an election and has *nexus* in Michigan, which means the taxpayer has a physical presence in Michigan for a period of more than 1 day during the tax year, actively solicits sales in Michigan and has gross receipts sourced to Michigan, or is a member or has an ownership interest or a beneficial interest in a flow-through entity, directly, or indirectly through 1 or more other flow-through entities, that has nexus in Michigan. For definitions of "actively solicits", "gross receipts", and "physical presence," see MCL 206.811.

When to File

The flow-through entity tax annual return is required to be filed by the ***last day of the third month after the end of the taxpayer's tax year***. For calendar filers, that date is March 31. If the due date falls on a weekend or holiday, the due date is the next business day. An annual return must be filed by an electing flow-through entity each year of the three-year period that the entity is subject to tax, even if the liability is zero.

Note: The member credits that relate to the tax year filed on this annual return must be ***paid by the 15th day of the 3rd month*** after the taxpayer's tax year end. Payments made after that date to cover liability on this return do not qualify as a credit for members' same tax year. However, those allocated amounts will be eligible to be claimed as credit on members' following year's income tax return.

Extension of Time to File. Flow-through entities may request an extension of time to file the annual tax return. An approved extension extends the due date for filing the annual return for an additional 6 months (until September 30 for calendar year filers). However, an extension only extends the time to file the return and does not extend the time to pay the tax. A flow-through entity requesting an extension must therefore ***pay its estimated tax liability by the initial due date of the return*** (but by the 15th day of the 3rd month after the tax year to qualify as a member credit for that same tax year). Interest and, if applicable, penalty, will accrue from the initial due date of the return until the tax is paid. To receive an extension of the Michigan return, a taxpayer must make a request on MTO. This application is required regardless of whether the taxpayer has an approved extension of their federal return from the Internal Revenue Service or the request for extension is based on good cause. Do not send a copy of the federal extension to Treasury; however, retain a copy for your records.

To apply for an extension, log into MTO at mto.treasury.michigan.gov and select the applicable business on the FTE Dashboard. Follow the links to "File/Pay/Amend a Tax Return" under the FTE Actions menu, then select "Extension" for the applicable tax year. Once the request is completed, the option to make an Extension Payment is available. Any required payment must be made on MTO by the original due date of the return, or the extension request will be denied.

How to File

The flow-through entity annual tax return can only be filed through Michigan Treasury Online (MTO). Returns submitted outside of MTO will not be accepted and may result in the accrual of penalty and interest.

What to file

State Forms. In addition to this form, the following supporting schedules must be filed:

- If applicable, Form 5773, *Schedule for Reporting Non-electing Flow-Through Entity Income*
- Form 5774, *Schedule for Reporting Member Information for a Flow-Through Entity*

*Do not send copies of K-1s. Treasury will request them if necessary.

Estimated Payments

If a taxpayer reasonably expects its annual liability to exceed $800, the taxpayer must make quarterly estimated payments. For calendar filers, payments are due April 15, June 15, September 15, and January 15. For fiscal year filers, payments are due the same dates that correspond to the due dates in the calendar year. Taxpayers are subject to penalty and interest for failure to pay estimated tax payments as required under the Revenue Act. Beginning with tax year 2022, penalty and interest will not be charged if the preceding year's liability was $20,000 or less and the taxpayer submitted payments in 4 equal installments, the sum of which equals the immediately preceding year's liability.

Tiered Structures

A tiered structure refers to a situation where a flow-through entity has at least one other flow-through entity as a member. Within a tiered structure, each flow-through entity that has business activity in Michigan may or may not elect to pay the Michigan FTE Tax. Special adjustments are necessary in computing the tax base for entities in tiered structures to ensure that all direct and indirect members receive an appropriate amount of credit and report the appropriate adjustments on their income tax returns. These adjustments also ensure that tax is not paid more than once on income flowing through the tiers.

Tax Base Adjustments. To prevent double taxation within a tiered structure, positive business income (a positive distributive share) from another entity that elects to pay the Michigan FTE Tax must be removed from the tax base of the filer. This adjustment is captured on line 3 of this return. Further, **a flow-through entity is prohibited from claiming a credit for tax paid by another electing flow-through entity**. Instead, credits are passed through via reporting between entities and members, to be claimed on member income tax returns.

Positive business income tax base from *non-electing* flow-through entities remains in the tax base of the filer. To ensure that non-electing income is properly taxed and sourced to Michigan, that income is first removed from the tax base, then added back to the tax base of the filer *after* statutory additions and subtractions and apportionment using the non-electing flow-through entity's sales factor. These related adjustments are captured on lines 3 and 23 of this return, as well as Schedule for Reporting Non-electing Flow-Through Entity Income, Form 5773.

In completing the return, each filer is also required to make certain Michigan-specific additions and subtractions in the computation of its tax base, as reported on lines 5-20 of this form. For a taxpayer that is a member of another flow-through entity, the amounts reported on these lines should **exclude** the filer's share of such additions and subtractions from another flow-through entity. The taxpayer's share of additions and subtractions from *non-electing* flow-through entities will be reported separately on Form 5773 and thereafter included with the amount reported on Line 23 of this return.

Reporting Between Tiers. Regardless of whether an entity elects into the Michigan FTE tax, each entity within a tiered structure must pass through and report to its members all of the relevant Michigan flow-through entity tax information from other flow-through entities. This will allow the information to be reported through the tiered structure to all direct and indirect members of electing flow-through entities, and ultimately to the recipients that need that information. For additional information about reporting requirements, see Treasury's FAQs or Notice Regarding the Implementation of the Michigan Flow-Through Entity Tax.

Tiered Structures Filing Example:
FTE A is directly owned by FTE C. FTE B is also directly owned by FTE C. FTE C is owned by Resident 1 and Nonresident 2. FTE A and FTE C elect to pay the Michigan FTE tax, and FTE B does not. On FTE C's return, it subtracts out its share of positive business income from both FTE A and FTE B on line 3. FTE C reports additions and subtractions on lines 5-20 of the return based on only its own activity. FTE C's share of the positive business income from FTE B, a *non-electing* entity, is reported on Form 5773 with this return. On that schedule, FTE C's share of additions and subtractions from FTE B's activity are applied, and the resulting business income tax base is apportioned to Michigan using FTE B's sales factor. Next, FTE C's share of FTE B's Michigan business income tax base is carried from the supporting schedule to the return and added in on line 23.

On FTE C's Schedule for Reporting Member Information, Form 5774, the following are separately reported for Resident 1 and Nonresident 2:

- Names and social security numbers
- Respective shares of income subject to tax on FTE C's return, which includes business income tax base attributable to FTE B and which is reported on line 26.
- Respective shares of the total tax liability reported on FTE C's return, line 27.

Outside of this return filing, FTE C has additional required reporting to its members. See the "Reporting Between Tiers" section.

Miscellaneous General Instructions

- Percentages should be carried out four digits to the right of the decimal point. Do not round percentages. For example, 24.154266 percent becomes 24.1542 percent. When converting a percentage to a decimal number, carry numbers out six digits to the right of the decimal point. For example, 24.154266 percent becomes 0.241542.
- Report all amounts in whole dollars. Round down amounts of 49 cents or less. Round up amounts of 50 cents or more. If cents are entered on the form, they will be treated as whole dollar amounts.

Line-by-Line Instructions

Line 1: Apportionment factor calculation. The business income tax base is apportioned to Michigan using a sales factor. To compute the sales factor, divide the total sales in Michigan during the tax year by the total sales everywhere during the tax year. The apportionment provisions under Chapter 3 of the Michigan Income Tax Act — those used by individual taxpayers with business income — should be used on this return.

Sales includes gross receipts from sales of tangible property, rental of property, proceeds from the sale of property used in the business and providing of services that constitute business activity. Exclude all receipts of nonbusiness income.

Sales of tangible personal property are in Michigan if:

1. The property is shipped or delivered to a purchaser (other than the United States government) within Michigan regardless of the free on board (F.O.B.) point or other conditions of the sale, or
2. The property is shipped from an office, store, warehouse, factory or other place of storage in Michigan and the purchaser is the United States government or the taxpayer is not taxable in the state of the purchaser.

NOTE: The numerator of the sales factor for individual income tax may include "throwback sales." *Throwback sales* are sales of tangible personal property that originate in Michigan, are made to a purchaser in another state or country and are "thrown back" to the numerator as Michigan sales because they are not taxable by the other state. Throwback sales follow federal P.L. 86-272 standards; the business must have physical presence in the other state or activity beyond solicitation of sales in order to exclude these sales into another state or country from the numerator. There is no "water's edge" for individual income tax purposes.

Sales of other than tangible personal property (e.g., services) are in Michigan if:

1. The business activity is performed in Michigan, or
2. The business activity is performed both in Michigan and in another state(s), but based on cost of performance, a greater proportion of the business activity is performed in Michigan.

There are special apportionment formulas for transportation companies and other authorized taxpayers. Those formulas are identified in Chapter 3 of the Michigan Income Tax Act.

Line 1a: Enter the taxpayer's sales sourced to Michigan, including throwback sales if applicable, made during the tax year.

Line 1b: Enter the taxpayer's total sales everywhere made during the tax year.

Line 2: Enter the taxpayer's business income, which means federal taxable income and includes payments and items of income and expense that are attributable to business activity of the taxpayer and separately reported to its members. Federal taxable income means taxable income as defined in section 63 of the internal revenue code without the deductions described under section 703(a)(2) of the internal revenue code. The deductions described in IRC 703(a)(2) which are excluded from the computation of federal taxable income the following common deductions:

- The deduction for personal exemptions;
- The deduction for charitable contributions;
- The deduction for net operating losses; and
- The deduction for depletion for oil and gas wells.

Flow-through entities should rely on federal forms and guidance for the computation of federal taxable income under IRC 63.

Special Instruction for S Corps: For purposes of computing federal taxable income only, S Corporations are treated as a corporation under IRC 1361(a)(2). S Corporations should accordingly compute federal taxable income by following the instructions and computations included within Form 1120 *US Corporation Income Tax Return*.

Special Instruction for Partnerships: For purposes of computing federal taxable income only, partnerships are treated as an association taxed as a corporation pursuant to an election under 26 CFR 301.7701-3(a). Partnerships should accordingly compute federal tax income by following the instructions and computations included within Form 1120 *US Corporation Income Tax Return*.

Business income includes items of income and expense attributable to the business activity of the taxpayer that are separately reported to its members (e.g., items reported on Schedule K-1). Many of these items will be included in the computation of federal taxable income under IRC 63; however, for any such items of income or expense not included in that calculation, that item should be included as an adjustment in the computation of business income and reported on this line.

Line 3: Enter the taxpayer's positive business income attributable to a distributive share from any other flow-through entity whose tax year ends with or within the taxpayer's tax year. Do not report negative business income attributable to other flow-through entities on this line. Each distributive share that is net positive from one flow-through entity should be reported here; do not net distributive shares from multiple flow-through entities together before reporting on this line.

Note: Positive business income tax base from non-electing flow-through entities in which the taxpayer is a direct or indirect member will be added back at a later point in the return (see Line 23). To ensure that the positive business income is correctly sourced to Michigan, that positive business income should be reported—and thus, removed from the tax base—on this line.

Additions

Taxpayers must report the following additions in completing their return. Report only the amounts from the taxpayer's business activity. **Do not include amounts from another flow-through entity**. See Line 23 for instructions on reporting the taxpayer's share of amounts received from a non-electing entity.

Line 5. Enter, to the extent excluded from federal taxable income, gross interest, dividends, and income from obligations or securities of states and their political subdivisions other than Michigan. This amount may be reduced by related expenses not allowed as a deduction by Sections 265 and 291 of the Internal Revenue Code (IRC).

Line 6. Enter, to the extent deducted in arriving at federal taxable income, losses on the sale or exchange of obligations of the US government, the income of which this state is prohibited from subjecting to a net income tax.

Line 7. Enter the total amount of charitable contributions deducted in arriving at federal taxable income.

Line 8. Enter the amount of taxes on or measured by net income, including taxes paid under the Michigan flow-through entity tax, to the extent deducted in arriving at federal taxable income.

Line 9. Enter gross expenses of producing oil and gas subject to the Michigan Severance Tax, 1929 PA 48, to the extent deducted in arriving at federal tax income.

Line 10. Enter, to the extent deducted in arriving at federal taxable income, gross expenses related to income derived from a mineral subject to the minerals severance tax under the Nonferrous Metallic Minerals Severance Tax Act, 2012 PA 410. A "mineral" is defined in Section 2(c) of the Nonferrous Metallic Mineral Extraction Severance Tax Act, MCL 211.782(c).

Line 11. There are no miscellaneous additions reported on this line.

Subtractions

Taxpayers must report the following subtractions in completing their return. Report only the amounts from the taxpayer's activity. **Do not include amounts from another flow-through entity.** See Line 23 for instructions on reporting the taxpayer's share of amounts received from a non-electing entity.

Line 14. Enter, to the extent included in federal taxable income, income from US government obligations (e.g., Series EE bonds, Treasury notes). This amount must be reduced by related expenses used to arrive at federal taxable income.

Line 15. Enter, to the extent included in federal taxable income, guaranteed payments paid for services rendered by a member who is an individual. Do not include guaranteed payments paid to members for the use of capital.

Line 16. Enter, to the extent included in federal taxable income, the amount of refunds received in the tax based on taxes paid under either the Michigan Flow-through Entity Tax or the City Income Tax Act, 1964 PA 284, MCL 141.501 to 141.787.

Line 17. Enter, to the extent included in federal taxable income, gross income from the production of oil and gas subject to the Michigan Severance Tax, 1929 PA 48.

Line 18. Enter, to the extent included in federal taxable income, gross income derived from a mineral subject to the minerals severance tax under the Nonferrous Metallic Minerals Severance Tax Act, 2012 PA 410. A "mineral" is defined in Section 2(c) of the Nonferrous Metallic Mineral Extraction Severance Tax Act, MCL 211.782(c).

Line 19. The use of this line is limited to the following scenarios:

- If business income on line 2 of this form is a loss (negative amount) but with a Michigan addition to income, the tax base is ultimately a positive number, report zero on line 2 and use this line to include the loss amount that should have been reported on line 2.
- **Partnerships:** If negative income (loss) needs to be reported for one or more partner(s) on form 5774, (e.g., because there is a special allocation of income, expense, gain, or loss as permitted under the internal revenue code) that loss cannot be reported on 5772. To reconcile the total of partner income on Form 5774 to Form 5772 as required, enter zero on form 5774 for all partners with a loss and use this line to report their negative income.

Tax Liability

Line 23. Enter the total amount of Michigan-sourced income from flow-through entities that have not elected to pay the Michigan Flow-through Entity Tax. **Do not include positive business income from flow-through entities that have elected to pay the Michigan Flow-through Entity Tax.** The amount reported here must be equal to the total Michigan-sourced income from non-electing flow-through entities reported on Form 5773.

Line 24. If the amount reported on this line is negative, then no tax is owed for this year. The flow-through entity tax does not allow for the carryback or carryforward of losses.

Line 25. The Michigan Flow-through Entity tax is only levied on the portion of the business income tax base allocable to members who are individuals, fiduciaries (trusts and estates), and other flow-through entities. Enter the business income tax base allocable to members subject to tax under the CIT (corporations, insurance companies, and financial institutions). The amount entered on Form 5774, Part 1, Total Reporting member Michigan income share of CIT.

Line 27. MTO will complete the math on this line, which must correspond with the total of Form 5774, Part 2. This amount on this line represents the total tax levied on, and paid by the filer, for the filer's tax year, which will be eligible for the filer's members' credit. **However, only the flow-through entity tax paid before the fifteenth day after the third month of the tax year (i.e., March 15 for calendar year filers) will be eligible to be claimed as a credit for the same tax year.** Flow-through entities must consider this payment date when reporting the proper amount of the credit to its members each year.

Payments, Penalties, and Tax Due

Line 28. Enter the total amount of estimated tax payments made throughout the year. If applicable, include on this line the amount of any payment submitted through MTO as part of the flow-through entity tax election.

Line 29. Enter the amount of tax paid with a request for extension.

Line 32. Enter the overdue tax penalty. Enter the overdue tax penalty. Use the following "Overdue Tax Penalty" Worksheet. Annual returns filed late or without sufficient payment of the tax due are subject to a penalty of 5% of the tax due for the first two months.

Penalty increased by an additional 5% per month, or fraction thereof, after the second month, to a maximum of 25 percent.

WORKSHEET – OVERDUE TAX PENALTY

A. Tax Due from Form 5772, Line 31. . . . ___________
B. Late/extension or insufficient payment penalty percentage . . . . ___________
C. Multiple Line A by Line B . . . . ___________

Carry the amount from line to Form 5772, Line 32.

Line 33. Enter the overdue tax interest. Use the following "Overdue Tax Interest" worksheet. For a list of interest rates, click on "Reports and Legal Resources" on the Treasury website at www.michigan.gov/treasury . Interest rates are updated in Revenue Administrative Bulletins (RABs).

WORKSHEET – OVERDUE TAX INTEREST

A. Tax Due from Form 5772, 31 . . . . ___________
B. Applicable daily interest percentage . . ___________
C. Number of days return was past due . ___________
D. Multiply Line B by Line C . . . . ___________
E. Multiple Line A by Line D . . . . ___________

Carry the amount from line to Form 5772, Line 33.

Line 35. Enter the overpayment to be refunded to the taxpayer. Taxpayers will not be permitted to use this amount as a credit forward to a subsequent tax return.

For More Information

See guidance published on Treasury's website at www.michigan.gov/taxes. A web page, FAQs, and several Notices have been published in relation to this tax.