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SINGLE BUSINESS TAX FOREIGN TAX BASE RETROACTIVITY

RAB 99-10. This Revenue Administrative Bulletin (RAB) describes how the Michigan Single Business Tax (SBT) applies to non-United States entities doing business in Michigan for tax years that begin before January 1, 2000.

ISSUES

- I.** Who is a “foreign person” for Single Business Tax purposes?
- II.** Is a foreign person required to file for Michigan Single Business Tax for tax years that begin before January 1, 2000 if the foreign person is not subject to United States federal income taxes for tax years that begin before January 1, 2000?
- III.** May a foreign person apply to the Department for a refund of Single Business Tax paid if the foreign person is not subject to United States federal income taxes for tax years that begin before January 1, 2000?
- IV.** How does a foreign person who is required to file a United States federal income tax return file for the Single Business Tax for tax years that begin before January 1, 2000?
- V.** How does a United States person with foreign business activity file for the Single Business Tax for tax years that begin before January 1, 2000?

CONCLUSIONS

- I. “Foreign Person” Defined.** For a corporation, partnership, or other type of business organization, a “foreign person” is a business entity or business organization formed under the laws of a foreign country or a political subdivision of a foreign country. For an individual such as a sole proprietor, a “foreign person” means an individual who is not a United States citizen or United States resident. “Foreign person” includes a person that is

either subject to or not subject to taxation under the United States Internal Revenue Code of 1986 as amended ("IRC"). "Foreign person" does not include a "United States person" as defined in the Single Business Tax Act ("SBTA").

II. Foreign Persons Not Subject to United States Federal Income Tax. A foreign person that is not subject to United States federal income taxes under the IRC and/or a provision in an applicable income tax treaty for tax years that begin before January 1, 2000 is not required to file a Single Business Tax return for those tax years, except for certain persons that are specifically subject to the SBT under MCL 208.22a; MSA 7.558(22a) (insurance companies) and MCL 208.35(c) (i), (ii) and (iii); MSA 7.558 (35) (certain nonprofit persons).

A. Foreign persons not required to file an SBT return for tax years that begin before January 1, 2000 include the following:

- 1) foreign persons not required to file a US 1120F, US 1040NR, or US 1065 or other applicable United States federal income tax form that are not subject to United States federal income taxes (except as noted in II, B below); or, a foreign person who files a United States tax return solely to claim protection under a provision in an income tax treaty that is not subject to United States federal income taxes;
- 2) persons with no United States permanent establishment under an applicable international income tax treaty, unless the person is subject to taxation under IRC 871(a) OR IRC 881 and the person conducts Michigan business activity;
- 3) foreign persons whose business activity is the operation of ships or aircraft used principally in international traffic that are not subject to United States income taxes under a provision of the IRC or an applicable income tax treaty;
- 4) foreign persons engaged in the operation of motor vehicles or a railway as a common carrier or contract carrier used to transport passengers or property between a point outside the United States and any other point that are not subject to United States income taxes under a provision of the IRC or an applicable income tax treaty;
- 5) foreign persons that are not subject to United States income taxes under a provision of the IRC or an applicable income tax treaty whose business activity is the use, maintenance, or rental of railway rolling stock, motor vehicles, trailers or containers used in the United States for a period or periods not expected to exceed in the aggregate 183 days in any twelve month period. However, a foreign person described in this subparagraph is subject to the Single Business Tax and federal income tax under the IRC if the business activity is attributable to a permanent establishment in the United States;
- 6) foreign persons not conducting a trade or business within the United States as defined in the IRC and that have no income derived from sources within the United States; and,

- 7) foreign persons with no business activity within Michigan as defined by MCL 208.3(2) and as described in RAB 1998-1, "Single Business Tax Nexus Standards."
- B. Foreign persons that are required to file an SBT return for periods that begin before 1/1/2000 include:
- 1) Certain nonprofit persons that are specifically subject to the SBT under MCL 208.35(c) (i), (ii), and (iii); MSA 7.558(35) notwithstanding that the person is exempt from United States federal income taxes under the IRC. These persons are federally tax exempt organizations under IRC 501(c)(12) [certain benevolent life insurance associations, mutual ditch or irrigation companies, mutual or cooperative telephone companies], IRC 501(c)(16) [certain corporations organized for financing crop operations], and IRC 501(c)(4) that would be exempt under IRC 501(c)(12) but for its failure to meet the requirements in IRC 501(c)(12) that 85% or more of its income must consist of amounts collected from members. These nonprofit organizations calculate their tax base under MCL 208.20; MSA 7.558(20).
 - 2) Insurance companies that calculate the tax base and adjusted tax base under MCL 208.22a; MSA 7.558(22a), whether or not the insurance company is subject to United States federal income taxes under the IRC.
 - 3) Persons subject to United States federal income taxes under the IRC. (See, Section IV of this RAB.)

III. Refunds

Taxpayers that are not required to file an SBT return described in this RAB who paid single business tax for tax years that begin before January 1, 2000 may be entitled to a refund, subject to the statute of limitations. MCL 205.27a (2); MSA 7.558(27a). A petition for refund shall state the reasons why the foreign person is not subject to United States federal income taxes under the IRC or an applicable tax treaty, and shall cite specific provisions of the IRC or tax treaty under which the taxpayer claims that it is not taxable. The claim shall include a copy of the U.S. federal form 1120F if the taxpayer was required to file one to claim a treaty-based exemption. The Department may require additional information or documentation to establish that the taxpayer is not subject to United States income taxes under the IRC for the applicable tax years.

IV. **Foreign Persons Subject to United States Federal Income Tax (1120F, 1040NR, or other foreign filers)**

A foreign person with business activity and nexus¹ in Michigan that is subject to United States federal income taxes under the IRC (with due regard to any applicable income tax treaty) for tax years that begin before January 1, 2000 is subject to the Single Business Tax. A person that is subject to United States federal income tax is subject to the SBT although the person's federal taxable income is zero or negative.

A. **Business Income** The foreign person's business income is federal taxable income as reported on the applicable federal form (including forms 1120F, 1120FSC, 1120L, 1120PC, 1065, 1040NR). The adjustments ("additions") to federal taxable income under MCL 208.9; MSA 7.558(9) are those adjustments related to federal taxable income as reported on the federal form. Federal taxable income includes: effectively connected income (IRC 882, OR IRC 871(B)); non-effectively connected income (investment type income under IRC 881 OR IRC 871(A)); income subject to branch profits tax (IRC 884); and income subject to personal holding company tax (reported on schedule PH, Form 1120).

For a foreign partnership, business income is the payments and items of income and expense which are attributable to United States business activity of the partnership and separately reported to the partners on U.S. federal form 1065. The SBTA states:

"Business income" means federal taxable income, except that for a person other than a corporation it means that part of federal taxable income derived from business activity. For a partnership, business income includes payments and items of income and expense which are attributable to business activity of the partnership and separately reported to the partners." MCL 208.3(3); MSA 7.558(3).

The partnership's "business income" is measured by the United States "federal taxable income" that the partners derive from the partnership as stated in MCL 208.3(3). Although partnerships are not taxed federally at the entity level, they are required to file U.S. federal form 1065. A foreign partnership that engages in a trade or business in the United States or has gross income derived from sources in the United States must file federal form 1065, even if its principal place of business is outside the United States or one or all its members are nonresident aliens. A foreign partnership's U.S. form 1065 reflects its income effectively connected to its United States trade or business and income derived from sources in the United States (not its worldwide income). Foreign partnerships are taxable persons under the Single Business Tax Act and calculate their business income in the same manner as a United States partnership.

¹ See Revenue Administrative Bulletin 1998-1, "Single Business Tax Nexus Standards," for tax jurisdiction standards that are applicable to foreign and United States taxpayers.

- B. Compensation.** Generally, compensation is remuneration of any kind paid to employees, officers, and directors for services connected to the United States business activity. Generally, for a foreign corporation compensation includes the wages and other remuneration deductible on federal corporation Form 1120F (compensation of officers, salaries and wages, pension, profit sharing plans, and employee benefit programs). However, the “wages” portion of compensation must be reported on a cash basis. The “non-wage” portion of compensation (“fringe benefits”) is reported on either a cash or accrual basis consistent with the taxpayer’s method of accounting for income tax purposes. For most filers this is the amount reported on federal Form 940 for the taxable year. In addition to amounts actually reported on the federal Form 940, compensation includes payments to non-resident alien individuals that are exempt from withholding under IRC 3401(a) (6) and regulations promulgated thereunder.
- C. Apportionment.** The pre-apportioned tax base of a foreign person consists of values attributable to sources within the United States as reported on the federal form. For corporations this is typically form 1120F (business income and adjustments) and compensation, generally as reported on the federal form 940, or if no form 940 is required, as deductible on form 1120F. The tax base from business activity and other sources within the United States is apportioned to Michigan by a formula under chapter 3 of the SBTA, MCL 208.40 to 208.69. Under this RAB, foreign persons report a tax base that is geographically limited to value added within the United States. This U.S.-only tax base is apportioned using the same formula as is used by U.S. persons for tax years that begin before January 1, 2000, which includes worldwide factors in the denominator. For tax years that begin on or after January 1, 2000, the denominators for the payroll factor, property factor, and sales factor include only U.S. payroll, property, and sales, as amended by 1999 PA 115.
- 1. Property Factor.** For a foreign person, the property factor is a fraction, the numerator of which is the average value of the taxpayer’s real and tangible personal property owned or rented by the taxpayer in Michigan during the tax year and the denominator of which is all of the taxpayer’s real and tangible personal property owned or rented everywhere during the tax year. MCL 208.46; MSA 7.558(46).
 - 2. Payroll Factor.** For a foreign person, the payroll factor is a fraction, the numerator of which is the total wages paid in this state by the taxpayer and the denominator of which is the total wages paid everywhere during the tax year by the taxpayer. MCL 208.49; MSA 7.558(49).
 - 3. The Sales Factor.** For a foreign person, the sales factor is a fraction, the numerator of which is the total sales of the taxpayer in Michigan during the tax year, and the denominator of which is the total sales of the taxpayer everywhere during the tax year. MCL 208.51; MSA 7.558(51). A sale of tangible personal property is within this state (a “Michigan sale”) if it is shipped or delivered to any purchaser within this state regardless of the free on board point or other conditions of the sale. MCL 208.52; MSA 7.558(52). A foreign person’s sales

factor numerator includes all sales that are shipped or delivered to a purchaser within Michigan, regardless of where the sale originates or the location from which the goods are shipped. For example: a foreign person that ships goods to a purchaser anywhere within Michigan from a plant or facility outside or within the United States includes the sale in the sales factor numerator. A foreign person's sales factor denominator includes all sales that are shipped or delivered to any purchaser. A "Michigan sale" other than a sale of tangible personal property (including the performance of services) is determined under MCL 208.53; MSA 7.558(53).

4. **Foreign Insurance Companies.** Foreign persons that calculate the tax base and adjusted tax base under MCL 208.22a (insurance companies) apportion the tax base under MCL 208.62; MSA 7.558 (62).
 5. **Transportation Services.** Foreign persons whose business activities consist of transportation services shall apportion the tax base under MCL 208.57; MSA 7.558(57) or MCL 208.58; MSA 7.558(58).
 6. **Foreign Financial Organizations.** A foreign financial organization shall apportion the tax base under MCL 208.65; MSA 7.558(65).
- V. **United States Persons.** The law is not changed for United States persons. For all tax years, an incorporated United States person with nexus in Michigan reports business income as federal taxable income as reported on the federal form 1120, 1120S or applicable corporate form. The compensation for all U.S. persons is worldwide compensation paid to all employees, officers, and directors. This includes amounts reported on the US federal form 940 and amounts paid to or for the benefit of the taxpayer's employees wherever located. Non-incorporated United States persons (sole proprietors, partnerships, or other business organizations) continue to report the tax base using the applicable federal form for that business such as the 1065, or 1040.

LAW AND ANALYSIS

Background

In 1999, the Michigan legislature enacted 1999 PA 115 to resolve questions regarding the application of the Single Business Tax to foreign persons and to make other amendments to the act. These changes were signed by the Governor on July 14, 1999, and the essential provisions apply to tax years beginning on or after January 1, 2000 (1/1/2000). The legislature did not expressly address the foreign tax base questions retroactively, and therefore this RAB explains the law for tax years that begin before January 1, 2000.

The SBTA imposes tax on the adjusted tax base of all persons with business activity within Michigan [MCL 208.31(1); MSA 7.558(31)]. Before 1999 PA 115 was signed into law, the Single Business Tax Act did not distinguish between foreign persons and United States persons. All taxpayers calculated the tax base without regard to geography. The Single Business Tax is

imposed upon that part of the adjusted tax base that is allocated or apportioned to Michigan under the provisions of MCL 208.40; MSA 7.558(40) to MCL 208.69; MSA 7.558(69). Taxation of extraterritorial value added is avoided by application of the formula that measures Michigan value added according to sales, payroll, and property attributable to Michigan in relation to sales, payroll, and property everywhere for most businesses. *Trinova Corp v Michigan Dep't of Treasury*, 111 S Ct 818, 498 US 358, 112 LEd2d 884. The SBTA provides other apportionment formulas for transportation businesses, financial institutions, and insurance companies.

The imposition of the SBTA is coextensive with the jurisdictional limitations imposed by the United States Constitution. The Constitutional limitations upon Michigan's Single Business Tax jurisdiction, or "nexus" standards, are explained in RAB 1998-1. Michigan has jurisdiction to tax all persons with business activity within its borders, without regard to whether the person is engaged in intrastate, interstate, or foreign commerce, or whether the person is a United States or foreign business. *Container Corporation of America v Franchise Tax Board*, 463 US 159 (1983); *Barclays Bank PLC v Franchise Tax Board*, 512 US 114 (1994); *Wardair v Florida Dep't of Revenue*, 477 US 1 (1986).

When the legislature enacted the SBT in 1975, it intended to tax the adjusted base of all persons with business activity in Michigan. The original SBTA stated: "There is hereby levied and imposed a specific tax of 2.35% upon the adjusted tax base of every person with business activity in this state which is allocated or apportioned to this state ." MCL 208.31(1); MSA 7.558(31).

Other than lowering the rate to 2.3% in 1994, and to 2.2% in 1999, the incidence and object of the tax stated in MCL 208.31(1); MSA 7.558(31) has not changed. For tax years beginning before January 1, 2000, the SBT does not explicitly distinguish between foreign and U.S. businesses in the imposition of the tax. Furthermore, "business activity" includes "intrastate, interstate, or foreign commerce" under MCL 208.3(2); MSA 7.558(3). However, in defining the adjusted tax base, the SBTA uses terminology from the IRC. Key federal terms include "federal taxable income" under IRC 63 and "wages" as defined under IRC 3401.

The federal terminology creates interpretive issues for some foreign entities, especially those that do not pay federal income taxes under the provisions of the IRC or under international tax treaties. The SBTA's silence with regard to a foreign person's tax base may imply that an entity that is not subject to U.S. federal income taxes has no federal taxable income, and therefore no "business income" for tax periods that begin before 1/1/2000. Business income for SBT purposes means "federal taxable income." MCL 208.3(3); MSA 7.558(3). "Federal taxable income means taxable income as defined in section 63 of the IRC." MCL 208.5(3); MSA 7.558. Therefore, by adopting the federal definition to define Michigan business income, the legislature indirectly limited the business income component of the SBT base to income that is subject to taxation under the IRC. For a foreign corporation, business income is federal taxable income reported on U.S. 1120F; for a foreign partnership it is the income reported on U.S. federal form 1065; and for a sole proprietor it is federal taxable income effectively connected to the United States trade or business or derived from sources within the United States as reported on U.S. federal form 1040NR. In addition, a taxpayer that earns income from a source within the United States that is taxed under IRC 871(a) or IRC 881 includes this income in business income for SBT purposes. Generally, the payer reports this income to the taxpayer and to the Internal Revenue Service on

federal form 1042-s or 1042. This income is included in business income whether tax is withheld under IRC 1441 or 1442 (and related federal regulations) or reported on US form 1120F.

In addition, differing interpretations exist as to whether a foreign person has “compensation” within the meaning of the SBTA, and if so, whether it includes U.S.-based compensation or worldwide compensation. The SBTA, MCL 208.4(3); MSA 7.558(4), defines compensation as all payments to employees, officers, or directors that are subject to or specifically exempt from withholding under the IRC. Literally, the tax imposed by IRC 3402 [United States federal wage withholding tax] applies to all wages paid worldwide by a domestic or foreign employer. IRC 3401(a)(6) and regulations promulgated thereunder expressly exempt wages paid to non-resident alien individuals. The wages described in IRC 3401(a)(6) are excluded from the definition of “wages” and therefore are not taxed. Therefore, it could be concluded that wages paid to a worker in a foreign country are “specifically exempt from” U.S. withholding tax, and are “compensation” for SBT purposes. This interpretation is consistent with the SBTA’s method of apportioning the entire value added tax base by a formula rather than by separate accounting. Under the formula, the Single Business Tax is applied to that part of the tax base that fairly represents the taxpayer’s business activity in this state.

It can also be argued under international jurisdictional norms that the wages paid to non-U.S. workers in foreign countries are neither subject to nor specifically exempt from the U.S. withholding tax. In other words, because the United States has no power to impose a withholding tax upon wages paid by an employer that is not subject to United States taxing jurisdiction, it is meaningless to consider whether such wages are “specifically exempt from” tax under IRC 3401 – 3406. Furthermore, the provisions in IRC 3401(a) (6) and regulations implicitly refer to wages paid by *U.S. taxpayers* (foreign or domestic) to non-resident alien individuals, typically those working in the United States who are residents of another country. The legal interpretations expressed in this and the preceding paragraph do not constitute positions of the Department of Treasury but are offered as examples of the context from which 1999 PA 115 arose.

The legislative clarifications to MCL 208.4(3); MSA 7.558(4) [compensation definition] are by implication effective for tax periods starting after the effective date of the act. This means that the legislation did not resolve the legal questions on “compensation” for past tax years. The Department interprets 1999 PA 115 consistent with the view that wages paid to non-resident alien individuals by non-U.S. taxpayers for past periods were neither subject to nor specifically exempt from U.S. wage withholding tax, and therefore were not included in compensation. However, wages paid by U.S. federal income taxpayers (foreign and domestic) were specifically exempt from withholding tax under IRC 3401(a)(6) and federal regulations, and therefore are included in compensation under MCL 208.4(3) for all relevant periods. For a foreign person, the United States taxing jurisdiction is limited to U.S. source business profits and other U.S. source income, therefore, the compensation component of the SBT is limited to the compensation related to the U.S. source income, which is generally the compensation that is deductible on the U.S. federal income tax form.

United States Persons

A business that is subject to United States federal income tax as a United States person must report its worldwide business income and worldwide compensation for SBT purposes. Generally, business income for corporations is federal taxable income as reported on the federal Form 1120 and compensation is amounts reported on the federal Form 940, except that the compensation includes all compensation paid everywhere, whether or not reported on a federal Form 940. The legislative changes regarding the foreign tax base that were enacted in 1999 PA 115 do not change the Department's interpretation of the law for these taxpayers. Detailed instructions for United States persons can be found in the Michigan Single Business Tax Forms and Instructions (available at www.treasury.state.mi.us).

Taxpayers Without a United States "Permanent Establishment"

For tax years beginning before January 1, 2000, a foreign person that is not subject to US federal income tax under the IRC or due to a provision in an income tax treaty (generally, a person without a permanent establishment in the United States) is not required to file a Single Business Tax return. However, certain nonprofit persons that are exempt from tax under the IRC are nevertheless subject to the Single Business Tax under MCL 208.35(c) (i), (ii), and (iii) [organizations described in IRC 501(c)(12) – certain benevolent life insurance associations, mutual ditch or irrigation companies, mutual or cooperative telephone companies; and IRC 501(c)(16) – certain corporations organized for financing crop operations]. These nonprofit organizations calculate their tax base under MCL 208.20; MSA 7.558 (20), which has been in effect since January 1, 1976. Furthermore, an insurance company calculates its tax base under MCL 208.22a without reference to federal taxable income for periods after August 3, 1987. Insurance companies calculate the tax base using a percentage of adjusted receipts without reference to federal taxable income. Foreign insurance companies and the specified nonprofit persons have had adequate statutory notice and guidance of their SBT filing responsibilities for all relevant tax years.

The recent, prospective amendments enacted by 1999 PA 115 to define "business income" for foreign persons creates an inference that the SBTA formerly failed to adequately define business income for foreign persons not subject to tax under the IRC or an applicable income tax treaty for periods beginning prior to January 1, 2000, except as noted above for certain nonprofit persons and foreign insurance companies as provided in MCL 208.20; MSA 7.558(20) and MCL 208.22a; MSA 7.558(22a).

The "addbacks" (additions and subtractions) under MCL 208.9; MSA 7.558(9) that are dependent on having federal taxable income are not included in the adjusted tax base of a person with no federal taxable income except as provided in MCL 208.20; MSA 7.558(20). The compensation addback in MCL 208.9(5); MSA 7.558 (9) is not dependent upon having federal taxable income. The legal analysis for the compensation component of the SBT base is discussed below.

Before the enactment of 1999 PA 115, the law was unclear regarding compensation paid to employees in foreign countries (nonresident alien individuals) by businesses with activity in Michigan but that were not subject to U.S. federal income taxes. The question is whether such

wages were “subject to or exempt from withholding under section 3401 to 3406 of the IRC” for those tax years. The legislative amendments to MCL 208.4(3) (1999 PA 115) have rendered that determination irrelevant for tax years that begin on or after January 1, 2000. After that time, compensation for all taxpayers is determined without regard to federal withholding law, although generally, taxpayers can determine domestic compensation with reference to federal withholding reporting methods (federal Form 940), with possible adjustments.

Due to the special circumstances faced by most foreign persons that were not required to file U.S. federal income taxes (including those protected by a tax treaty) and the context from which this legislation arose, the legislative changes strongly imply that these foreign persons lacked sufficient statutory guidance as to whether they were subject to the SBT. These foreign persons had no business income or adjustments related to federal taxable income and generally had no obligation to withhold tax from wages under IRC 3402. Therefore, except as otherwise stated in this RAB, foreign taxpayers not required to pay U.S. federal income tax under the IRC or by an applicable income tax treaty before January 1, 2000 are not required to file an SBT return for periods beginning before January 1, 2000. A reference in this RAB to a “treaty,” an “income tax treaty,” or an “applicable income tax treaty” means a properly ratified income tax treaty between the United States and another national government under which the taxpayer has rights to claim protection from United States federal income taxes. The Department’s interpretation contained in Single Business Tax Questions and Answers M15 is hereby retroactively rescinded. (Question and Answer A6 remains rescinded).

Foreign Persons With a United States Permanent Establishment

For tax years beginning before January 1, 2000, a foreign person that properly reports U.S. federal income tax on a federal form 1120F, 1065, 1040NR, or other applicable federal form can report business income as federal taxable income as reported on the federal form. In most cases, compensation for a foreign person filing federal form 1120F is total compensation reported on the federal Form 940. In addition to amounts reported on the federal Form 940, compensation includes amounts paid to nonresident alien individuals working within United States that are specifically exempt from withholding under IRC 3401(a)(6) and regulations promulgated thereunder. (See section IV, subparagraph B of this RAB.) Compensation also includes all remuneration in any form that is deductible on the federal form 1120F, 1065, or 1040NR.

Tax Treaties

The United States has entered income tax treaties with many countries. In general, tax treaties are designed to avoid international double taxation at the national level and do not limit Michigan’s jurisdiction to tax business activity within its borders. The treaties are relevant to the Michigan Single Business Tax Act because it adopts the term “federal taxable income” from the United States IRC to define “business income.” The treaties affect the SBT indirectly, to the extent that they limit federal taxable income. Under IRC 894(a)(1), the IRC applies to a taxpayer “with due regard to any treaty obligation of the United States which applies to such taxpayer.” Therefore, a person that has no federal taxable income under the IRC or under a tax treaty has no business income for SBT purposes, except for certain non-profit entities and insurance

companies whose tax base is not dependent upon having federal taxable income under MCL 208.20; MSA 7.558(20) or MCL 208.22a; MSA 7.558(22a). Treaties also prohibit taxation of profits from specific business activities, such as transportation activities (discussed below).

Permanent Establishment

Tax treaties prohibit the federal taxation of business profits earned by a foreign person unless the profits are attributable to a permanent establishment in the taxing nation. (Treaties also contain provisions on other types of income.) “Permanent establishment” is a term of art and is defined differently in some tax treaties. In general, a permanent establishment is a fixed place of business such as a place of management, a branch, an office, a factory, or a mine. In addition, a dependent agent with authority to conclude contracts may constitute a permanent establishment with or without a “fixed place of business” under some treaties. A subsidiary corporation does not create a permanent establishment on behalf of the parent-corporation merely by virtue of the relationship. It is important that a foreign person consult the terms of an applicable treaty under which it is entitled to claim protection in order to determine its taxability in the United States, and under the SBT for tax years that begin before January 1, 2000.

United States Taxing Jurisdiction under the IRC

If no treaty is in effect under which the taxpayer can claim protection, the IRC applies without modification by treaty. The jurisdictional standard under the IRC is lower than under a tax treaty. That is, treaties give greater protection from taxation than under the IRC alone. In general, the IRC imposes tax on foreign persons that conduct a “trade or business” in the United States and/or that derive income from sources within the United States. IRC 871(A), IRC 871(B), IRC 881, IRC 882, IRC 884. In addition, the IRC imposes tax on the United States source gross transportation income of certain foreign persons under IRC 887, but exempts certain gross income from international operation of ships or aircraft under IRC 883. Any income that is taxable under the IRC is “business income” within the meaning of MCL 208.3(3); MSA 7.558(3). Therefore, a foreign person that lacks a United States permanent establishment has “business income” for SBT purposes if it has income that is taxed under IRC 871(a) or IRC 881. Such person would be subject to the SBT if it has nexus and business activity in Michigan.

Prior Departmental Interpretations

This RAB retroactively rescinds the department’s interpretation contained in SBT Questions and Answers M15. Furthermore, all other interpretations, rulings, or positions, published or unpublished, are also rescinded to the extent they are in conflict with this RAB as they relate to the SBT liability of a foreign person.

Definitions

“Form 1120” means the form 1120 "U.S. Corporation Income Tax Return " for the relevant tax year published by the United States Department of Treasury, Internal Revenue Service.

“Form 1120F” means the form 1120F "U.S. Corporation Income Tax Return of a Foreign Corporation" for the relevant tax year published by the United States Department of Treasury, Internal Revenue Service.

“Form 940” means the form 940 “Employees Annual Federal Unemployment (FUTA) Return” for the relevant tax year published by the Department of Treasury, Internal Revenue Service.

“MCL” means Michigan Compiled Laws.

"MSA" means Michigan Statutes Annotated.

“PA” is an abbreviation for the term “public act.” Public acts are laws enacted by the people of the State of Michigan by and through the elected legislature and governor. The term public act derives from the Michigan Constitution of 1963, Article IV, Section 23.

“SBT” means the Michigan Single Business Tax, 1975 PA 228, MCL 208.1, et seq.

“SBTA” means the Michigan Single Business Tax Act, 1975 PA 228, MCL 208.1, et seq. as amended.

“1999 PA 115” is a public act that amended of the Michigan Single Business Tax Act (1975 PA 228) that includes provisions on the tax base of foreign persons.