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**REVENUE ADMINISTRATIVE BULLETIN 2015-20**

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**CORPORATE INCOME TAX  
WHERE BENEFIT OF SERVICES IS RECEIVED**

Pursuant to MCL 205.6a, a taxpayer may rely on a Revenue Administrative Bulletin issued by the Department of Treasury after September 30, 2006, and shall not be penalized for that reliance until the bulletin is revoked in writing. However, reliance by the taxpayer is limited to issues addressed in the bulletin for tax periods up to the effective date of an amendment to the law upon which the bulletin is based or for tax periods up to the date of a final order of a court of competent jurisdiction for which all rights of appeal have been exhausted or have expired that overrules or modifies the law upon which the bulletin is based.

**RAB 2015-20**

The Corporate Income Tax (“CIT”) Act<sup>1</sup> sets forth rules for determining a taxpayer's sales in this state, which are used to calculate the sales factor for purposes of apportioning the taxpayer's CIT tax base.<sup>2</sup> The statute sets forth specific rules regarding the circumstances under which sales from the performance of services are wholly or partially attributable to Michigan. Specifically, the CIT Act provides that sales from the performance of services should be sourced to Michigan if the recipient of the services receives the benefit of the services in this state.<sup>3</sup>

This Revenue Administrative Bulletin (“RAB”) addresses how a taxpayer determines where the recipient of services receives the benefit of those services, for purposes of calculating the apportionment sales factor. This RAB does not address the sourcing of other types of sales under the CIT Act.

**ISSUES**

- I. What does the statute provide with respect to sourcing sales from the performance of services?
- II. Can the recipient of services be someone other than the purchaser of the services?
- III. How does a taxpayer determine where the recipient of services receives the benefit of those services? What if only a portion of the benefit is received in this state?
- IV. How will the Department's guidelines be applied in practice?

<sup>1</sup> MCL 206.601 et seq.

<sup>2</sup> MCL 206.665.

<sup>3</sup> MCL 206.665(2)(a).

- V. What if a taxpayer is unable to determine where the recipient of a service received the benefit of that service?

## CONCLUSIONS AND ANALYSIS

### I. What does the statute provide with respect to sourcing sales from the performance of services?

Section 665 of the CIT Act sets forth rules for determining a taxpayer's sales in this state, which are used to calculate the sales factor for purposes of apportioning the taxpayer's CIT tax base.<sup>4</sup> Subsection (2) of that section provides, in relevant part:

(2) Sales from the performance of services are in this state and attributable to this state as follows:

(a) Except as otherwise provided in this section, all receipts from the performance of services are included in the numerator of the apportionment factor if the recipient of the services receives all of the benefit of the services in this state. If the recipient of the services receives some of the benefit of the services in this state, the receipts are included in the numerator of the apportionment factor in proportion to the extent that the recipient receives [the] benefit of the services in this state.<sup>5</sup>

The sourcing of sales derived from certain specific types of services, such as securities brokerage services and telecommunications services, are addressed separately in section 665, but the general rule set forth in section 665(2)(a) applies to receipts received from the performance of most other services.<sup>6</sup>

### II. Can the recipient of services be someone other than the purchaser of the services?

Yes. Section 665 of the CIT Act sources sales from the performance of services in reference to the "recipient of the services."<sup>7</sup> While in many cases the recipient of the services under consideration will also be the purchaser of those services, the statutory language indicates that the recipient of the services may, in fact, be someone other than the purchaser of those services.

### III. How does a taxpayer determine where the recipient of services receives the benefit of those services? What if only a portion of the benefit is received in this state?

All the benefit of a service is received in this state if any of the following guidelines apply:

- 1) The service relates to real property that is located entirely in this state.

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<sup>4</sup> MCL 206.665.

<sup>5</sup> MCL 206.665(2)(a).

<sup>6</sup> See Part V of this RAB for discussion of special sourcing provisions.

<sup>7</sup> MCL 206.665(2)(a).

- 2) The service relates to tangible personal property that (a) is owned or leased by the purchaser and located in this state at the time that the service is received, or (b) is delivered to the purchaser or the purchaser's designee(s) in this state.
- 3) The service is received in this state and provided to a purchaser who is an individual physically present in this state at the time that the service is received.
- 4) The service is received in this state and is in the nature of a personal service, such as consulting, counseling, training, speaking, and providing entertainment, that are typically conducted or performed first-hand, on a direct, one-to-one or one-to-many basis.
- 5) The service is provided to a purchaser that is engaged in a trade or business in this state and relates only to the trade or business of that purchaser in this state.
- 6) The service relates to the use of intangible property such as custom computer software, licenses, designs, processes, patents, and copyrights, which is used entirely in this state.

As stated in the statute, if the recipient of the service receives only a portion of the benefit of the service in this state, then the receipts are included in the apportionment factor in proportion to the extent that the benefit of the service is received in this state.<sup>8</sup> Accordingly, the following guidelines should be used by taxpayers, to the extent applicable, to properly apportion a service where the recipient of the service receives only a portion of the benefit of the service in this state:

- 7) If the service relates to real property that is located in this state and in one or more other states, the benefit of the service is received in Michigan to the extent that the real property is located in Michigan.
- 8) If the service relates to tangible personal property that (a) is owned or leased by the purchaser and located in this state and in one or more other states at the time that the service is received, or (b) is delivered to the purchaser or the purchaser's designee(s) in this state and in one or more other states, the benefit of the service is received in Michigan to the extent that the tangible personal property is located in Michigan, or is delivered to the purchaser or the purchaser's designee(s) in Michigan.
- 9) If the service is provided to a purchaser that is engaged in a trade or business in this state and in one or more other states, and the service relates to the trade or business of that purchaser in this state and in one or more other states, the benefit of the service is received in Michigan to the extent that it relates to the trade or business of the purchaser in Michigan.
- 10) If the service relates to the use of intangible property such as custom computer software, licenses, designs, processes, patents, and copyrights, which is used in this state and in one or more other states, the benefit of the service is received in Michigan to the extent that the intangible property is used in Michigan.

If a fact pattern encountered by a taxpayer is not addressed by a specific guideline, the taxpayer should use the guideline that is most closely applicable to the fact pattern at issue.

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<sup>8</sup> MCL 206.665(2)(a).

In determining the extent to which the benefit of a service is received in Michigan, a taxpayer may use any method to apportion the benefit between Michigan and one or more other states, provided that the method is reasonable and appropriate in light of all existing facts and circumstances, that the taxpayer applies the chosen method uniformly and consistently, that the same or a similar method is used to apportion services that are substantially similar, and that the chosen method is supported by the taxpayer's business records as they existed at the time that the service was provided or the revenue therefrom was received by the taxpayer. See, for instance, Example C which uses percentage of total number of rental units to determine the extent to which the benefit of a service is received in Michigan; square footage may also have been a reasonable and appropriate measure.

The taxpayer must maintain adequate documentation, through its books and records, supporting its determination regarding where the benefit of a service performed was received, and the means or method used by the taxpayer to determine the extent of the benefit received in Michigan.

#### **IV. How will the Department's guidelines be applied in practice?**

The following are examples of the application of the guidelines set forth above.

##### Example A.

A real estate development firm from State A is developing a tract of land in Michigan. The real estate development firm from State A engages a surveying company from State B to survey the tract of land in Michigan. The survey work is completed and the plats are drawn in Michigan and delivered to the real estate development firm in State A. All of the surveyor's gross receipts from the surveying services are attributable to Michigan and are included in the numerator of the apportionment factor because the surveying services relate to real property that is located in Michigan. See guideline 1 above.

##### Example B.

A corporation headquartered in State Y is building an office complex in Michigan. The corporation from State Y contracts with an engineering firm from State X to oversee construction of the buildings on the site. The engineering firm performs some of its services in Michigan at the building site, and some of its services in State X. All of the gross receipts from the engineering services are attributable to Michigan and included in the numerator of the apportionment factor because the services relate to real property that is located in Michigan. See guideline 1 above.

##### Example C.

A company headquartered in State Y which owns apartments in both Michigan and State A contracts with a pest control company to provide pest control services. One contract is entered into, which covers 100 apartment units in Michigan, and 400 apartment units in State A. Twenty percent (100/500) of the gross receipts from the pest control contract are attributable to Michigan

and included in the numerator of the apportionment factor because twenty percent of the apartment units covered by the contract are located in Michigan. See guideline 7 above.

Example D.

An automated machinery manufacturer located in State B sends a representative to Michigan to perform on-site repairs on a machine owned by its customer and located at the customer's Michigan plant. All of the gross receipts from the repair service are attributable to Michigan and included in the numerator of the apportionment factor because the service provided relates to tangible personal property that is owned by the purchaser and located in this state at the time that the service is received. See guideline 2(a) above.

Example E.

A corporation located in Michigan performs mail services for a customer located in State X. The mail activities consist of the mailing of materials provided by the customer to households located throughout the United States. The corporation located in Michigan performs some of the activities related to the mail contract in State X. Five percent of the mailings are sent to addresses within Michigan. Five percent of the gross receipts related to the services covered by the mail contract are attributable to Michigan and included in the numerator of the apportionment factor because five percent of the mailings are delivered directly to the purchaser's customers in this state. See guideline 8(b) above.

Example F.

A Michigan company contracts with a company from State F to test the engine compression of its aging fleet of trucks. At the time the testing is performed, all but two of the trucks are parked at the equipment garage located at the Michigan company's headquarters. One truck is at an offsite repair shop in Michigan where the compression test will be conducted. Another truck is kept in State Z where the testing will be done. The gross receipts received for the compression testing services will be sourced to Michigan for the testing done on the fleet of trucks located at the Michigan company's headquarters because the testing was performed on tangible personal property located in Michigan at the time the service was received. The service performed on the truck at the offsite repair shop will also be sourced to Michigan because the testing was done on the truck located at the offsite Michigan repair shop. The receipts for the testing performed on the truck located in State Z will be sourced to State Z. See guideline 8(a) above.

Example G.

A resident from State O receives a haircut at a Michigan salon while vacationing in Michigan. All of the receipts from the salon services are attributable to Michigan and included in the numerator of the apportionment factor because the services were provided to an individual physically present in Michigan. See guideline 3 above.

Example H.

A small toy manufacturing company located in Michigan sells its products in Michigan and State W. The company has sales offices with marketing personnel in both states. All sales agents attend the company's annual sales meeting, which is held in Michigan. The toy company hires a Michigan entertainment company to provide a pianist and a band to entertain during meals and

other events at the sales meeting. All of the entertainment company's receipts from the engagement are attributable to Michigan and included in the numerator of the apportionment factor because the entertainment services were received in Michigan, are in the nature of personal services, and were performed first-hand. See guideline 4 above.

Example I.

A small consulting company based in State T that provides consulting and training services to businesses is retained by a Michigan company to speak to its sales force about improving customer service. To lower costs, the speech is delivered via teleconference. The speaker remains in State T, while the sales force listens to the speech from their regular work locations at the company's two sales offices, located in Michigan and in State O. The consulting company's receipts from the speaking services are apportionable to Michigan and to State O, and are included in the numerator of the apportionment factor in proportion to the extent that the benefit of the services is received in Michigan. Apportioning between the states by the number of telephone participants may be one, but not necessarily the only, reasonable and appropriate method. See guideline 9 above.

Example J.

A Michigan widget manufacturer hires a book-binding company located in State N to bind the instruction manuals for the company's widgets. The bindings and printed materials are supplied by the widget manufacturer. The book-binding company's receipts from the services are attributable to Michigan and included in the numerator of the apportionment factor because the services were provided to a purchaser engaged in business only in Michigan, and relate to the business of the purchaser in Michigan. See guideline 5 above.

Example K.

A corporation from State A contracts with a computer software company from State D to develop and install a custom software application in a business office of the corporation from State A located in Michigan. The software firm does consulting work on the project in State A and in Michigan. The software development is performed in State D and in Michigan. The software package is delivered to the corporation from State A at the business office in Michigan. All of the gross receipts from the software development services are attributable to Michigan and included in the numerator of the apportionment factor because the services relate to the use of intangible property that is used entirely in Michigan. See guideline 6 above.

Example L.

A software company located in Michigan provides technical support services to its customers, which are located throughout the United States, through a call center in Michigan. The typical customer telephones the call center to resolve an issue with software that they are using on their desktop. Seven percent of the calls handled by the call center originate from Michigan. Depending on other facts and circumstances, seven percent of the gross receipts from the support services provided by the call center are attributable to Michigan and included in the numerator of the apportionment factor because seven percent of the call center services relate to the use of computer software which is used in this state. See guideline 10 above.

**V. What if a taxpayer is unable to determine where the recipient of a service received the benefit of that service?**

The statute provides special sourcing rules with respect to many specific types of sales of services, including securities brokerage services, interest from loans secured by real property, fees from loan servicing, and receipts from credit card receivables.<sup>9</sup> Certain of the specific sourcing rules contain discrete default provisions. For example, when sourcing receipts from securities brokerage services, receipts are sourced to Michigan if the sales of securities services are to customers within Michigan. However, the statute further provides that if receipts can be associated with a particular customer, but it is impractical to associate the receipts with the customer's address (for instance, because the customer's address is not known), then the customer's address is presumed to be the address of the branch office that generates the customer transactions.<sup>10</sup>

If a receipt from the sale of services is not addressed by a specific statutory subsection, the CIT Act states that the receipt is sourced based on where the benefit to the customer is received or, if where the benefit to the customer is received cannot be determined, to the customer's billing address.<sup>11</sup> This RAB provides guidelines that taxpayers should use when sourcing receipts from sales of services that are not addressed by one of the specific statutory subsections. A taxpayer may not simply use the customer's billing address to source a sale of services without first making a reasonable and demonstrable effort, based on its books and records, to determine the location where the recipient of the service received the benefit of that service. In addition, pursuant to section 669, sales are not excluded from the apportionment factor if the location of the recipient's benefit cannot be determined.

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<sup>9</sup> MCL 206.665(2).

<sup>10</sup> MCL 206.665(2)(b).

<sup>11</sup> MCL 206.669.