



## Legal Alert: Michigan Supreme Court Upholds the Compact Election

July 14, 2014

On July 14, 2014, the Michigan Supreme Court in a splintered 3-1-3 decision found in favor of IBM's election to apply the Multistate Tax Compact's three-factor apportionment formula to the now-repealed Michigan Business Tax (MBT).

### Background

Several states, including Michigan in 1970, entered into the Multistate Tax Compact (Compact), which describes how multistate corporations allocate and apportion income. One provision of the Compact is an election that allows corporations to elect annually to apply the apportionment rules contained in the Compact (rather than state apportionment rules that deviate from the Compact). Michigan's single sales factor apportionment formula for the MBT deviated from the Compact, and IBM elected to apply the Compact's equally weighted, three-factor formula.

The Michigan Department of Treasury (the Department) rejected IBM's election on several grounds, including that the Compact was repealed by implication as part of the MBT enactment in 2008. The Michigan Court of Appeals found in favor of the Department, and IBM appealed to the Michigan Supreme Court.

### Michigan Supreme Court Decision

A divided Michigan Supreme Court issued three separate opinions on two distinct issues. A "lead opinion" and dissenting opinion were each supported by three justices. A concurring opinion joined in the result described in the lead opinion.

As to the election, four Michigan Supreme Court justices (the lead and concurring opinions) found that IBM was entitled to make the Compact election and use the Compact's three-factor formula for its 2008, 2009 and 2010 tax years. Additionally, all seven justices held that the Modified Gross Receipts Tax component of the MBT is an "income tax" for purposes of the Compact (in addition to the Business Income Tax component of

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the MBT, which is also an “income tax”).

While the concurring opinion embraced the result contained in the lead opinion, it also relied on another basis to allow IBM to make the election. The concurrence determined that the Michigan legislature reenacted the election when it passed several pieces of legislation in 2011 to enact a new corporate income tax.

**Sutherland Observations:**

The Court’s holding was based on its ability to harmonize the two seemingly conflicting apportionment provisions. The court interpreted the Compact election as being compatible and capable of co-existing with Michigan’s apportionment regime for the tax years 2008 through 2010. In doing so, several key questions were not determined by the majority of the justices, including whether the legislature impliedly repealed the election and whether Michigan could unilaterally repeal the Compact.

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