

Michigan provides guidance regarding Corporate Income Tax unitary business group control test and relationship tests

January 18, 2013

In brief

The Michigan Department of Treasury describes the control test and the two alternative relationship tests that must be satisfied in order for two or more qualified United States persons to qualify as a unitary business group (UBG) under Michigan's Corporate Income Tax (CIT). [Michigan Department of Treasury [Revenue Administrative Bulletin 2013-1](#), *Corporate Income Tax, Unitary Business Group Control Test and Relationship Tests* (1/7/13)]

In detail

RAB 2013-1 describes the control test and the two alternative relationship tests described in the state's income tax law (MCL 206.611(6)). If a group of entities satisfies the control test as described in the statute, and if that same group also satisfies one of two relationship tests, that group of entities will constitute a UBG.

The control test

RAB 2013-1 provides the following guidance, along with examples, regarding the control test.

- The control test is satisfied when one person owns or controls, directly or indirectly, more than 50% of

the ownership interests, with voting or comparable rights, of other person or persons.

- Entities that satisfy the CIT control test constitute 'controlled groups of entities,' which include: (1) parent-subsidiary controlled group of entities; (2) brother-sister controlled group of entities; and (3) combined controlled group of entities. Excluded ownership interests and controlled group of entities without common control are also discussed.
- Voting agreement presumptions exist in determining whether the ownership interests owned

by a person possess voting (or comparable) rights.

- Rules are provided for determining the voting rights in entities without stock or other forms of ownership interests, such as nonstock, nonprofit organizations.
- The RAB provides guidance regarding an entity that may be included in more than one controlled group of entities.
- Indirect ownership considerations are addressed relating to: family; attribution to and from partnerships, corporations, trusts, and estates; and options. General operating

principles of the indirect ownership rules are also discussed.

Relationship test - flow of value

In addition to satisfying the control test, a UBG must meet one of two alternative relationship tests. One relationship test provides that a group of persons must have business activities or operations that result in a flow of value between or among persons in the group.

The RAB recognized that the US Supreme Court described a unitary business as requiring "some sharing or exchange of value not capable of precise identification or measurement - beyond the mere flow of funds arising out of a passive investment." In determining whether a flow of value exists, a relevant question in the inquiry is whether contributions to income result from: (1) functional integration, (2) centralization of management, and (3) economies of scale. The RAB provides guidance regarding each of these three elements.

Relationship test - contribution/dependency

The second alternative relationship test provides that a group of persons must have business activities or operations that are integrated with, dependent upon, or contribute to each other. This occurs under many of the same circumstances as the flow of value test. Where the facts indicate that business activities are conducted and managed under one centralized system, there is evidence that the entities are dependent upon each other or that they contribute to each other such that the elements of a unitary business group are present.

Factors demonstrating a flow of value or dependency

As noted above, a flow of value exists when contributions to income result from: (1) functional integration, (2)

centralization of management, and (3) economies of scale.

The following factors may support a finding of functional integration:

- Intercompany sales, exchanges, or transfers of intangibles, services, or products between business entities.
- Transfers of technical information, know-how, trade secrets, research and development or other intangibles that are significant to the operations or activities of the entities.
- The sharing and use of any administration, accounting, payroll, inventory control, or distribution systems that are controlled through a common network.
- Purchases of substantial quantities of goods, services, or intangibles significant to the entities' sales or operations, particularly if the purchases result in cost savings.
- Common marketing that results in mutual advantage.
- Common intercompany financing.

The following factors may evidence economies of scale:

- Centralized purchasing designed to achieve savings through volume, timing of purchases, or interchangeability of parts.
- Centralized administrative functions such as legal services, accounting, payroll, human resources, and employee benefit administration.

Centralized management exists when common officers or management participate in decision making for the various entities. When an integrated executive force appears to exist that

has control over major policy decisions, this factor is evidence but not conclusive that centralized management exists.

Special application considerations

The RAB provides additional guidance regarding the following special UBG application considerations.

- *Application of links in a chain within a group.* It is not necessary for all entities to have a direct relationship connection with every other entity for a unitary group to exist. It is sufficient if the relationship is indirect.
- *Instant unity.* Whether the unitary relationship can arise instantly depends on the surrounding facts and circumstances. The RAB addresses the control and relationship tests in the context of instant unity with regard to acquired entities and newly formed entities.

Examples

The RAB provides two lengthy examples (Examples 16 and 17) that demonstrate factors that could support a finding that a UBG exists.

The takeaway

The guidance in RAB 2013-1 regarding UBGs under the Corporate Income Tax is substantially similar to guidance provided by the Department regarding UBGs under the Michigan Business Tax in [RAB 2010-1](#), *Unitary Business Group Control Test*, and [RAB 2010-2](#), *Unitary Business Group Relationship Tests*.

Notable differences in RAB 2013-1, as compared to the Michigan Business Tax RABs, include the following:

- Some examples under the control test replace general or limited

partnerships or LLCs with corporations.

- Example 4 provides that ownership can be measured through a partnership even though a partnership is not included in the UBG. Similar indirect ownership concepts are reflected in new examples 12 and 14.
- New examples 13 and 15 provide guidance around indirect ownership.
- The existence of centralized management is expanded to

include the role of management of an entity or entities in the affairs of its affiliates and whether a management process is applied to other entities. For example, the business 'guidelines' established by a parent for its subsidiaries, the 'consensus' by which a parent's management process was involved in the subsidiaries' business decisions, and the oversight and other assistance provided by a parent to its subsidiaries all point to centralized management.

- Regarding instant unity, RAB 2013-1 provides that there is no specific time requirement that dictates when a person becomes a member of a unitary business group. Whenever both the control test and one of the two relationship tests are met, that person must file as a member of the UBG and it remains a member of that group so long as the control test and one of the two relationship tests continue to be met.

Let's talk

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