

Michigan Files Motion for Rehearing and Motion to Stay in *IBM*; Legislators Explore Retroactive Legislation That Would Disallow “Compact” Election

August 15, 2014

Overview

On July 14, 2014, the Michigan Supreme Court in *International Business Machines v. Michigan Department of Treasury* (“*IBM*”) held that the taxpayer could elect to compute both the Modified Gross Receipts Tax and the Business Income Tax components of its 2008 Michigan Business Tax (“MBT”) liability using the Multistate Tax Compact (“Compact”) election in lieu of the 100% sales-weighted apportionment formula under the MBT Act.¹ By application of the election (Compact Article III), the taxpayer was allowed to use an equally-weighted, three-factor apportionment formula (property, payroll and sales).²

In response to the *IBM* decision, the Michigan Department of Treasury (“Treasury”) filed two motions with the court: a Motion for Rehearing, requesting that the court reconsider its decision; and a Motion to Stay, asking that the court suspend the effects of the case pending the outcome of the Motion for Rehearing. Also, some Michigan legislators have apparently begun to consider a legislative response aimed at retroactively disallowing the Compact election.

In this Tax Alert we summarize Treasury’s two motions and the potential legislative response to the court’s decision. We also provide some taxpayer considerations in light of the potential for retroactive legislation.

Motion for Rehearing / Motion to Stay

On August 4, 2014, Michigan Attorney General Bill Schuette, together with Michigan Solicitor General Aaron D. Lindstrom, filed a Motion for Rehearing, asking the Michigan Supreme Court to reconsider its opinion in *IBM*.³ The Motion for Rehearing contends that a fundamental error exists in the lead opinion’s holding that the MBT Act did not repeal by implication the Compact election. The motion argues further that if left unaltered, the impact of the decision would cost the State of Michigan a “budget-busting aggregated refund . . . to mostly out-of-state corporations.”⁴

The Attorney General also filed on August 4 a companion Motion to Stay the July 14, 2014 decision, requesting that the Michigan Supreme Court stay the effects of its holding on all lower court cases pending the outcome of the rehearing request. The motion states that there are approximately 134 Compact election cases pending before the Michigan Tax Tribunal and Michigan Court of Claims, as well as numerous others at the administrative appeal level. The motion estimates that if these cases are decided in favor of the applicable taxpayers, the total potential financial impact would be approximately \$1.098 billion plus interest.⁵

On August 11, 2014, the taxpayer filed its Response in Opposition to Treasury’s Motion for Rehearing and Treasury’s Motion to Stay. The Response contends that: (1) Treasury is merely rearguing the “rejected claim” that the MBT Act impliedly repealed the Compact election, and (2) any projected financial impact on Michigan is irrelevant.⁶

¹ *International Business Machines v. Michigan Department of Treasury*, Mich. Supreme Court Docket No. 146440 (July 14, 2014).

² The background, judicial history and implications of the *IBM* decision were discussed in detail in the [Deloitte Tax Alert dated July 16, 2014](#).

³ *International Business Machines v. Michigan Department of Treasury*, Motion for Rehearing of Appellee Department of Treasury of the State of Michigan (August 4, 2014).

⁴ *Id.* at 3.

⁵ *International Business Machines v. Michigan Department of Treasury*, Motion to Stay the July 14, 2014 Opinion and Motion for Immediate Consideration (August 4, 2014).

⁶ *International Business Machines v. Michigan Department of Treasury*, Response in Opposition to Treasury’s Motion for Rehearing and Treasury’s Motion to Stay the July 14th Opinion (August 11, 2014).

Possible Retroactive Legislation

In the wake of these developments, Michigan legislators appear to be exploring a legislative remedy to neutralize the impact of the Michigan Supreme Court's decision in *IBM*.⁷ One potential legislative option would be the enactment of an amendment to MCL § 205.581 that would explicitly eliminate the ability for a taxpayer to make the Compact election, *retroactive to January 1, 2008*.⁸ The legislature could also amend relevant provisions of the MBT Act (MCL §§ 208.1101 *et seq.*) to specifically disallow the Compact election beginning January 1, 2008.

While questions exist regarding whether such retroactive tax legislation would survive scrutiny under the Due Process Clause of the U.S. Constitution,⁹ it should be noted that in 2010 the Michigan Court of Appeals upheld retroactive sales and use tax legislation, which had been enacted in 2007 to avoid the application of a taxpayer-friendly Michigan Supreme Court decision in *Betten Auto Center*.¹⁰

Taxpayer Considerations

As some Michigan lawmakers explore legislation that, if enacted, would seek to retroactively repeal the availability of the Compact election, taxpayers may wish to consider whether there are options that may allow them to preserve their ability to make the election. While many taxpayers that have challenged Treasury's disallowance of the Compact election on previously-filed MBT returns have typically requested an Informal Conference (pursuant to MCL § 205.21(2)(b)) at the administrative hearing level, Treasury may attempt to argue that that approach does not protect against retroactively adopted law. On that note, however, several Michigan-based tax attorneys have commented, informally, that taxpayers who receive a Michigan court decision rendered prior to the enactment of retroactive tax legislation may be more favorably positioned to defend against the retroactive application of that legislation. Accordingly, taxpayers may wish to discuss with Michigan tax counsel whether it may be advantageous to withdraw from the administrative hearings process and instead file a petition with the Michigan Court of Claims.

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⁷ *Michigan Senate Leader Scrutinizing Multistate Tax Compact*, Amy Hamilton, Tax Analysts, State Tax Today, August 11, 2014.

⁸ A retroactive (to January 1, 2008) amendment to MCL § 205.581 was first proposed in 2010 in House Bill 6351, but was not enacted.

⁹ In addition to Due Process considerations, any explicit legislative repeal or limitation upon the Compact election provisions may also be subject to challenge under federal compact law and the Contract Clause of the U.S. Constitution. Michigan has been a member of the Multistate Tax Compact since 1970.

¹⁰ *Betten Auto Center v Dept. of Treasury*, 478 Mich. 864; 731 N.W.2d 424 (2007).