

STATE OF MICHIGAN
COURT OF APPEALS

LARRY J. WINGET and ALICIA J. WINGET,
Petitioners-Appellants,

UNPUBLISHED
October 16, 2012

v

DEPARTMENT OF TREASURY,
Respondent-Appellee.

No. 302190
Tax Tribunal
LC No. 00-319852

Before: TALBOT, P.J., and WILDER and RIORDAN, JJ.

PER CURIAM.

Petitioners appeal as of right from an order of the Michigan Tax Tribunal (MTT) affirming respondent's assessments for tax years 2001 and 2002. For the reasons set forth below, we affirm.

Petitioner Larry Winget is the sole shareholder of several subchapter S corporations. Most of the S corporations operate exclusively within Michigan, but during the tax years at issue, two or three S corporations had multistate operations. Petitioners determined their Michigan income tax liability by combining the property, payroll, and sales figures for all of the S corporations to calculate a single apportionment percentage. Petitioners applied this apportionment percentage to each of the S corporations. After reviewing petitioners' tax returns for tax years 2001 and 2002, respondent concluded that petitioners should have calculated and applied separate apportionment percentages for each of the S corporations. The MTT ruled in favor of respondent, and petitioners now appeal.

In the absence of fraud, we review the MTT's decision for "misapplication of the law or adoption of a wrong principle." *Briggs Tax Serv, LLC v Detroit Pub Schs*, 485 Mich 69, 75; 780 NW2d 753 (2010). Issues of statutory interpretation are reviewed de novo. *Id.*

Under the federal constitution, a state is prohibited from imposing income tax on value earned outside the state's borders. *Container Corp of America v Franchise Tax Bd*, 463 US 159, 164; 103 S Ct 2933; 77 L Ed 2d 545 (1983). When a state attempts to impose income tax on a multistate entity, obvious practical problems arise with identifying, separating, and apportioning in-state value and out-of-state value. *Id.* at 164-165. The United States Supreme Court has approved the "unitary business principle" to determine a multistate entity's apportionable share. *Allied-Signal, Inc v Dir, Div of Taxation*, 504 US 768, 778; 112 S Ct 2251; 119 L Ed 2d 533 (1992). But in order "for a business or individual to exercise multi-state apportionment, there

must “be 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 or a distinct business operation—which renders formula apportionment a reasonable method of taxation.” *In re Estate of Wheeler*, ___ Mich App ___; ___ NW2d ___ (Docket No. 302251, issued July 31, 2012), slip op, p 3, quoting *Container Corp*, 463 US at 166.

In accordance with the unitary-business principle, MCL 206.103, during the relevant tax years, provided the following:

Any taxpayer having income from business activity which is taxable both within and without this state, other than the rendering of purely personal services by an individual, shall allocate and apportion his net income as provided in this act.¹

The apportionment formula is set forth in MCL 206.115. At the time relevant to this appeal, MCL 206.115 read as follows:

All business income, other than income from transportation services shall be apportioned to this state by multiplying the income by a fraction, the numerator of which is the property factor plus the payroll factor plus the sales factor, and the denominator of which is 3.

“The property, payroll, and sales factors represent the percentage of the total property, payroll, or sales of the business used, paid, or made in this state.” *Grunewald v Dep’t of Treasury*, 104 Mich App 601, 606; 305 NW2d 269 (1981), citing MCL 206.116, MCL 206.119, MCL 206.121.

Petitioners argue that apportionment of “business income” under MCL 206.115 may be calculated by adding the property, payroll, and sales of multiple S corporations to establish a single property factor, a single payroll factor, and a single sales factor. We disagree. Our recent decision in *Malpass v Dep’t of Treasury*, 295 Mich App 263; 815 NW2d 804 (2011), dictates the outcome of this case.

In *Malpass*, the plaintiff individuals (i.e., natural persons) owned two separate S corporations. *Id.* at 265-266. The S corporations were allegedly “functionally integrated,” *id.* at 267, but nevertheless remained “separate and legally distinct business entities,” *id.* at 270. One S corporation conducted its business in Michigan, and the other S corporation conducted its business in Oklahoma. *Id.* at 265-266. The Michigan S corporation had a net gain, while the Oklahoma S corporation had a net loss. *Id.* at 266-267. In their amended tax returns, the taxpayers treated the S corporations “as a unitary business and applied the Michigan apportionment factors to both companies as a unitary business.” *Id.* at 266. By treating the S corporations as a single unitary business, the taxpayers were able to substantially reduce their

¹ Effective January 1, 2012, this statute was modified by replacing “as provided in this act” with “as provided in this part.” 2011 PA 38.

Michigan income tax obligations by applying the losses from the Oklahoma S corporation against their Michigan income. *Id.* at 266-267.

We held that the individuals were not permitted to treat the two S corporations as a unitary business, stating in relevant part as follows:

Plaintiffs argue in this case that they are allowed to apportion their income from [the S corporations] because the two corporations form a unitary business. . . . [T]here is no doubt that [the S corporations] have many characteristics of a unitary business. However, *they remain separate and legally distinct business entities, and nothing in the ITA allows for combined-entity reporting.* [*Id.* at 270 (emphasis added, citation omitted).]

Thus, *Malpass* stands for the proposition that “Michigan law does not allow separate entities to be treated as a unitary business in the absence of some common ownership at the entity level, and that being owned by the same individual taxpayers is insufficient to trigger this relationship requirement.” *Wheeler*, ___ Mich App at ___ (slip op at 4).

In this case, it is undisputed that petitioner’s S corporations are legally separate and distinct business entities and that there was no common ownership at the entity level. As a result, the S corporations do not form a single-business entity, and respondent correctly determined that petitioners were required to apply a separate apportionment percentage to each S corporation, depending upon the S corporation’s unique property, payroll, and sales figures.

Affirmed.

/s/ Michael J. Talbot
/s/ Kurtis T. Wilder
/s/ Michael J. Riordan