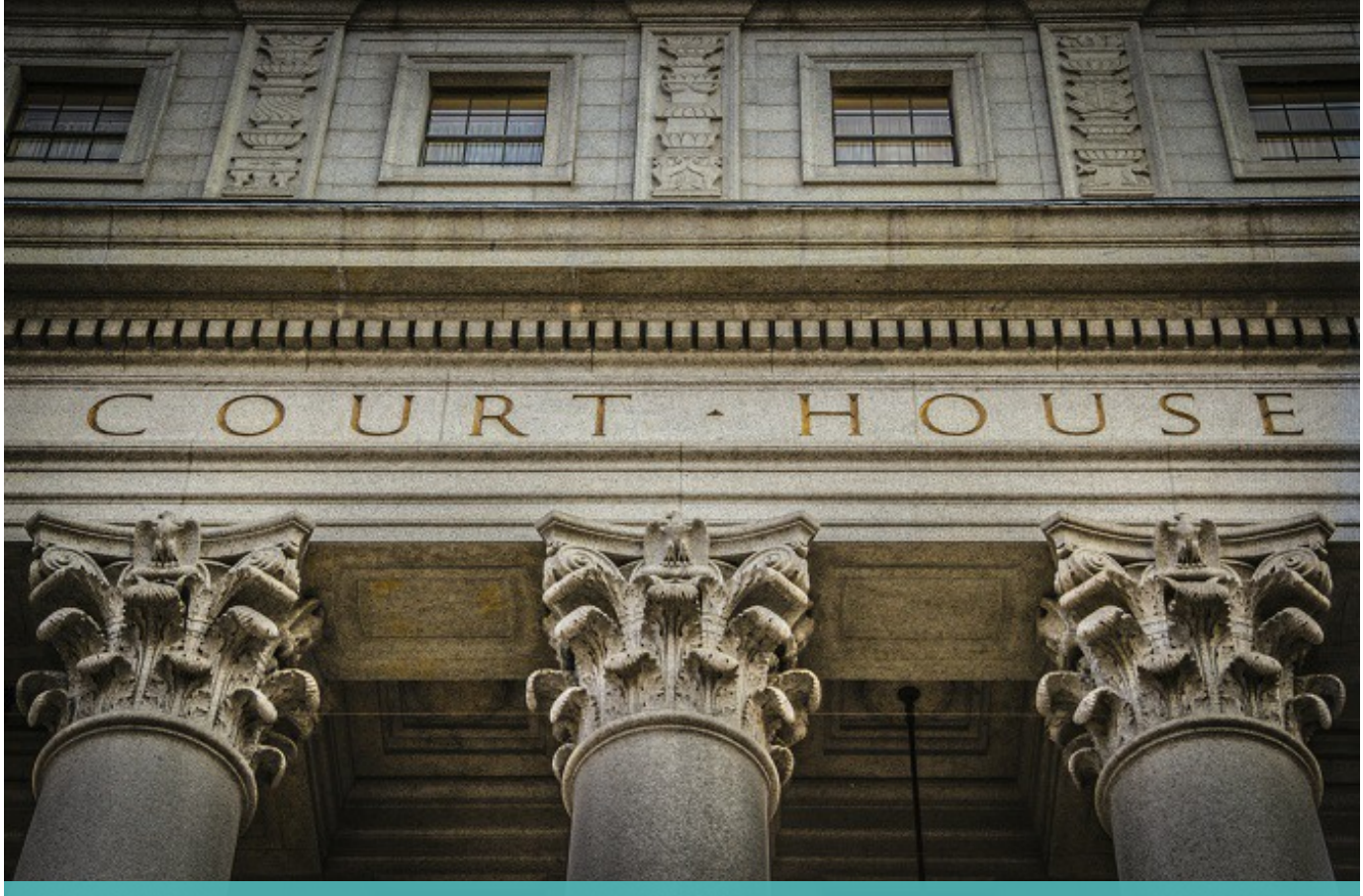


## Michigan: Treasury Department used wrong definition in determining whether a unified business group existed



David M. Kall | Friday, April 15, 2016

In the case [\*LaBelle Management, Inc. v. Michigan Department of Treasury\*](#), decided March 31, 2016, the Michigan Court of Appeals reversed a trial court's conclusion that three companies made up a unified business group in accordance with the federal income tax definition of constructive ownership. Instead, the Court of Appeals determined that the federal definition did not apply, and held that the trio of companies did not constitute a unitary business group.

### Background

Three different entities are involved: the plaintiff, LaBelle Management; The Pixie Inc.; and LaBelle Limited Partnership. During the relevant tax periods, two brothers owned LaBelle Management, a Michigan corporation, but neither owned more than 50 percent of the firm's common stock.

Pixie is also a Michigan corporation. Originally, LaBelle Management was a subsidiary of Pixie, but Pixie sold all of its interest in 2008, triggering the tax events in question. LaBelle Limited Partnership is a Michigan limited partnership, formed by the brothers' equal contributions. Later, the brothers' children were added to the partnership, reducing the brothers' shares.

After Pixie sold LaBelle Management, it reported its business tax as a company separate from Pixie. When the Michigan Department of Treasury conducted an audit for the tax years at issue, it determined that all three entities should be treated together, as a unitary business group. The treasury based its

## Michigan Treasury Department used wrong definitio

---

determination on the definition of a unitary business group in the [Michigan Business Tax Act](#) and interpretation of the act's language in a [2010 Administrative Bulletin](#).

The act's definition requires more than 50 percent ownership, directly or indirectly, for a unitary business group to exist. The bulletin provides a test for assessing whether an entity satisfies the tests for a unitary business group, and if it does, it is considered a single taxpayer and must file a combined tax return.

### **The department's analysis**

After applying the tests set forth in the bulletin, the Department of Treasury concluded that plaintiff LaBelle Management indirectly owned 100 percent of Pixie and LaBelle Limited Partnership, and that Pixie indirectly owned 100 percent of plaintiff LaBelle Management and 90 percent of LaBelle Limited Partnership. The Department of Treasury billed plaintiff LaBelle Management for \$11,856.29, accounting for tax payments already made.

Plaintiff LaBelle Management argued that the three companies did not constitute a unitary business group as defined by the Business Tax Act. The parties agreed that none of them directly owned more than 50 percent ownership interest of any of the others, so the operative question was whether there was sufficient indirect ownership or control to satisfy the statutory definition of a unitary business group.

In reaching its conclusion, the Department of Treasury looked to the federal income tax code's definition of constructive ownership for its consideration of the indirect-ownership-or-control-question.

### **The appellate court's analysis**

This is where the trial court went wrong. According to the appellate court, "federal tax statutes and regulations are replete with examples that illustrate the proposition that indirect ownership and constructive ownership are two different concepts."

Instead, the trial court should have construed the word indirect "according to its ordinary and primarily understood meaning." In its inquiry, the appellate court examined definitions in the New Oxford American Dictionary, Merriam-Webster's Collegiate Dictionary, Black's Law Dictionary, and the Fletcher Cyclopedia of the Law of Corporations, and concluded that "indirect ownership in [the Act] means ownership through an intermediary..."

Thus, the appellate court concluded, "no unitary business group exists because none of the involved entities (plaintiff [LaBelle Management], Pixie, and LaBelle Limited Partnership) owns, through an intermediary or otherwise, more than 50 percent of any other entity."



**David M. Kall**

[Team member bio](#)