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A little-noticed tax case the Michigan Supreme Court decided in July could have huge financial implications for the state — costing it more than \$1 billion.

In a 4-3 opinion, the court overturned two lower courts, ruling in favor of IBM and against the Michigan Treasury Department in a long-standing tax dispute about how corporations that do business in several states may calculate their Michigan taxes.

The ruling means IBM gets a \$6-million tax refund for 2008, rather than the \$1.3 million calculated by Michigan Treasury.

But the ruling has implications for many more companies and also could affect Michigan Business Tax cases in the 2009 and 2010 tax years.

And the case has implications beyond Michigan, but Michigan is the first state where a Supreme Court has ruled in favor of out-of-state corporations at the expense of the state Treasury, said Amy Hamilton, a senior writer for Tax Analysts, a publication that caters to tax professionals in law and accounting firms.

The Treasury Department estimates the state's exposure from the decision at \$1.1 billion, plus interest. Just what trickle-down effect the ruling may have on the state's programs — and ultimately residents — is not yet known. But officials say it would be felt.

In a strongly worded post-opinion motion seeking a rehearing of the case, Attorney General Bill Schuette said the ruling “results in the state potentially owing a budget-

busting aggregated tax refund in the hundreds of millions of dollars (not including

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and Budget, said officials believe most of the impact would be felt in the 2011-12 fiscal year, though there could also be some impact this year.

"It creates a significant problem for the budget," Weiss said. "We are hoping for reconsideration from the Supreme Court."

It's exceedingly rare for the Michigan Supreme Court to reverse one of its own opinions in a rehearing.

And an appeal to the federal courts does not appear to be an option, said Dave Murray, a spokesman for Gov. Rick Snyder.

Justice David Viviano wrote the majority opinion in favor of IBM, joined by Justices Michael Cavanagh and Stephen Markman, and by Justice Brian Zahra, who wrote a separate concurring opinion. Justice Bridget McCormack wrote the dissent, siding with the Treasury Department, joined by Chief Justice Robert Young Jr. and Justice Mary Beth Kelly.

At the heart of the cases are state corporate income tax policies designed to favor local corporations at the expense of out-of-state corporations, Hamilton said. The Michigan Business Tax, which was repealed in 2011, required out-of-state corporations to calculate their taxes based on sales, she said.

But since 1970, Michigan has belonged to a multistate compact, intended to make things easier for out-of-state corporations by providing greater uniformity in how they calculate their tax bills for various states.

Under the compact, corporations have the option of using the state tax law or an optional formula that considers not just sales but the property and payroll a corporation has in a given state.

Weighing in those factors generally leads to lower income tax bills for out-of-state

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The Legislature “had full knowledge of the compact and its provisions” when it passed the MBT, yet it “left the compact's election provision intact.”

In fact, the court suggested the Legislature shot itself in the foot in 2011, when it amended the legislation related to the multistate compact to say that starting Jan. 1, 2011, out-of-state corporations no longer had the option of using the three-pronged method to calculate state taxes.

If the Legislature hadn't wanted corporations to use that method in 2008, 2009 or 2010, it would have made the 2011 statute fully retroactive, the court said.

The ruling arguably gives out-of-state corporations better tax treatment than those located in Michigan.

In her dissent, McCormack said the MBT law and the compact law are “irreconcilably in conflict” and it makes sense to follow the law that is more specific and passed more recently — the MBT.

The Michigan case received no attention in the mainstream media, but corporate number crunchers have been watching. Accounting firms such as Deloitte have sent out alerts to clients in the wake of the Michigan ruling, letting them know the case could reduce tax liability for certain corporations.

“That's a huge chunk of money for any state and that's why it's been watched so closely,” Hamilton said.

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