TAXATION

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I. SINGLE BUSINESS TAXES

A. Tyson Foods Incorporated v. Michigan Department of Treasury

In a case of first impression,[1] the Michigan Court of Appeals determined that the Revenue Act provides the statutory authority for the Department of Treasury to issue more than one tax assessment to a corporation due to its failure to file tax returns for the tax years at issue, even though the taxpayer had paid the assessed taxes, penalties and interest due.[2] Plaintiff, Tyson Foods Incorporated (the "taxpayer"), had filed a complaint in the Court of Claims seeking a refund of tax, interest and penalties that had been paid under protest.[3] The taxpayer had submitted a motion for summary disposition which had been granted by the court of claims, and the Department of Treasury ("the Department")

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1. 276 Mich. App. 678, 741 N.W.2d 579 (2008).
2. *Id.* at 691, 741 N.W.2d at 586.
3. *Id.* at 682, 741 N.W.2d at 581.

appealed the granting of the motion to the court of appeals.[4] At issue was whether or not the Department could issue a second assessment for the same tax period and same single business taxes at issue for which it had previously issued a tax assessment to the taxpayer, and which the taxpayer had paid in full.[5] The taxpayer claimed that the Department did not have the authority, either under the Single Business Tax Act or the Revenue Act, to issue a second assessment when the Department had already issued an assessment for such taxes.[6] The taxpayer's position was that the first assessment issued was final and conclusive (hereinafter referred to as the "original assessment" to distinguish it from the "subsequent assessment"), and therefore, the Department was precluded from issuing a subsequent single business tax assessment for the same period.[7] The court of claims agreed with the taxpayer and ruled that the "[d]efendant had no authority to reassess [p]laintiff's Single Business Tax liability under the statutory authority granted to it" and that defendant "must accordingly refund those monies . . . [that] [plaintiff] paid under protest."[8]

The Department appealed this decision, arguing that it was authorized by law to impose assessments on taxpayers for taxes lawfully owed and that such authority was not limited to a single assessment for each tax period.[9] Plaintiff asserted, however, that once a "single business tax assessment" has been issued, the Department would be precluded from issuing subsequent assessments for the same tax period.[10] The court of appeals acknowledged that resolution of the issue required analysis of the Revenue Act, as well as the applicable provisions of the Single Business Tax Act.[11] The court phrased its analysis as "whether the relevant sections of the Revenue Act permit defendant to issue a second assessment to a corporate taxpayer for the same tax period in order to recover all the single business taxes lawfully owed to the state by the taxpayer."[12] The court of appeals found that the Department did indeed have such authority.[13]

In its analysis, the court of appeals noted that the taxpayer failed to voluntary comply with its obligation to file single business tax returns

4. *Id.* at 682-83, 741 N.W.2d at 581.
5. *Id.* at 683-84, 741 N.W.2d at 582.
6. *Id.*
7. *Tyson Foods*, 276 Mich. App. at 682, 741 N.W.2d at 581.
8. *Id.*
9. *Id.* at 683-84, 741 N.W.2d at 582.
10. *Id.* at 684, 741 N.W.2d at 582.
11. *Id.*
12. *Id.* at 685, 741 N.W.2d at 583.
13. *Tyson Foods*, 276 Mich. App. at 685, 741 N.W.2d at 583.

and, later, upon assessment, failed to file such returns even when it was specifically requested to do so by the Department upon payment of the original assessment.[14] The taxpayer had been requested to file the returns after it paid the original final assessment.[15] After payment by the taxpayer, the Department audited the taxpayer, and discovered that additional tax was due for the outstanding years at issue.[16] Based on this information, a subsequent final assessment was issued by the Department.[17] It was this subsequent final assessment that the taxpayer protested to the court of claims.[18] The court of appeals held that not permitting the defendant to issue a subsequent assessment would have allowed the taxpayer to evade its single business tax liability that was lawfully owed and due to the state.[19] Indeed, the court of appeals noted that any other interpretation would render M.C.L. Section 205.27(a)(2)[20] nugatory.[21] Finally, the court noted that it would "be an injustice and would prejudice the public interest to permit a corporation to benefit from its failure to file tax returns, which by law, it is obligated to file."[22]

The point stressed by the court was that if the taxpayer had filed its single business tax returns when first requested in the original notice of intent to assess, the Department might have reached a different conclusion; however, because the taxpayer had failed to file its returns (upon whatever basis or ground that it might have believed justified such non-filing), the actions of the defendant's auditor, that later determined that the taxpayer owed additional taxes, justified the issuance of a subsequent final assessment.[23] Although the taxpayer had paid the amounts in the original final assessment in full, the failure of the taxpayer to file the returns precluded the statute of limitations from

14. *Id.* at 686-87, 741 N.W.2d at 584. The taxpayer had not filed returns for the periods believing that it did not have the requisite "nexus" or connection with the state to subject the taxpayer to the state's jurisdiction to tax. Subsequently, the taxpayer determined that it did have the requisite nexus, and upon issuance of a final assessment, paid the tax originally assessed. *Id.*

15. *Id.* at 687, 741 N.W.2d at 584.

16. *Id.*

17. *Id.*

18. *Id.* at 681-82, 741 N.W.2d at 581.

19. *Tyson Foods*, 276 Mich. App. at 685, 741 N.W.2d at 583.

20. MICH. COMP. LAWS ANN. § 205.27(a)(2) (West 2003).

21. *Tyson Foods*, 276 Mich. App. at 685, 741 N.W.2d at 583 (citing Apsey v. Mem'l Hosp., 477 Mich. 120, 131, 730 N.W.2d 695, 701 (2007) ("A statute is rendered nugatory when an interpretation fails to give it meaning or effect.")).

22. *Id.* at 686, 741 N.W.2d at 583 (citing People v. Derror, 268 Mich. App. 67, 73-74, 706 N.W.2d 451 (2005)).

23. *Id.* at 687, 741 N.W.2d at 584.

running.[24] Therefore, the tax periods remained open for assessment, and the defendant was permitted by law to issue a subsequent assessment.[25] The taxpayer argued that its agreement in full with the original final assessment—via full payment of the original final assessment—made the original final assessment "final and conclusive."[26] However, the court noted that "the legislature plainly intended to permit defendant to issue a second tax assessment to a taxpayer . . . if necessary for defendant to collect the entire amount of taxes due from a taxpayer for the tax period at issue."[27]

One could argue that perhaps the Department should have audited the taxpayer prior to issuing its original final assessment, and thus could have avoided the need to issue a subsequent final assessment. However, the court of appeals considered this by noting that perhaps the Department had not done its job as efficiently as it could have, while also recognizing that "it is neither good government nor good policy to permit the Department of Treasury to have a seemingly unlimited power to issue multiple tax assessments to a taxpayer for the same tax period."[28] On the other hand, however, the court of appeals was more convinced that due to the taxpayer's conduct in failing to "voluntarily comply with its obligations to file,"[29] such conduct was so deficient that it did not preclude the defendant from issuing a subsequent final assessment for the same tax period if such action was necessary to collect the entire amount of taxes lawfully due.[30] Indeed, the court noted that had the plaintiff filed its returns it may have been able to avail itself of a four-year statute of limitations period for the assessment of tax deficiencies under M.C.L. Section 205.27(a)(2).[31] However, due to the plaintiff's failure to file the returns, the statute never began to run, and with an open statute of limitations period, the Department was legally authorized to issue a subsequent final assessment in order to collect taxes lawfully due.[32]

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24. *Id.* at 692, 741 N.W.2d at 586.

25. *Id.* at 687, 741 N.W.2d at 584; *see also* MICH. COMP. LAWS ANN. § 205.21(1) (West 2003).

26. *Id.* at 690, 741 N.W.2d at 585.

27. *Tyson Foods*, 276 Mich. App. at 688, 741 N.W.2d at 584-85.

28. *Id.* at 691, 741 N.W.2d at 586 n.8.

29. *Id.*

30. *Id.* at 691, 741 N.W.2d at 586.

31. *Id.* at 692, 741 N.W.2d at 586 n.8.

32. *Id.* at 691, 741 N.W.2d at 586 ("[W]hile the amounts in [the original final] assessment would be final and could no longer be challenged, the defendant would still have the authority to issue further assessments as necessary to collect the . . . tax owed by the corporate taxpayer to the state.").

The court went on further in its analysis and stated that even if the Department's original final assessment had been final and conclusive under M.C.L. Section 205.22,[33] it would only be found to be conclusive with respect to the specific assessment itself, and not with respect to the taxpayer's overall single business tax liability for the period at issue.[34]

Several distinguished practitioners have suggested that the power of the Department to issue a subsequent final assessment could be a trap for unwary taxpayers, with which they should be concerned.[35] While this may be true, as are all new cases of first impression, what should be emphasized in this case is that taxpayers are well advised to file their returns, especially when requested to do so by the Department. We now know that the payment of an assessment does not begin the tolling of a statue of limitations, only the filing of a return can do so.[36] While the failure to file the returns in this case may have been a decision influenced by risk control, regardless of the reason for not doing so, only the filing of the returns would have acted to begin the tolling of the statute of limitations.[37] Without the statute being tolled, the Department's ability to issue a subsequent final assessment was not precluded.[38] This is particularly so in light of the fact that the taxpayer did not protest the subsequent final assessment as to the amount of tax to be due and owing, for which there did not appear to be any material issue of fact.[39]

B. NSK Corporation v. Department of Treasury

In this matter before the court of appeals,[40] the issue was when interest should begin to accrue in favor of a taxpayer once an overpayment of tax is discovered, and whether additional statutory

33. *See generally* MICH. COMP. LAWS ANN. §§ 205.22(4)-(5) (West Supp. 2007).

34. *Tyson Foods*, 276 Mich. App. at 691, 741 N.W.2d at 586. In reading the provisions of M.C.L. § 205.21(1) and M.C.L. § 205.27(a)(2) together, the court concluded that "the Legislature plainly intended to permit defendant to issue a second tax assessment" if it was necessary in order for the defendant to collect the entire amount of taxes lawfully due from the taxpayer. *Id.* at 688, 741 N.W.2d at 584-85.

35. Samuel J. McKim, III & Joanne B. Faycurry, *A Malpractice Trap for Unwary Taxpayer Advisors "Settling" State Tax Disputes with the Michigan Department of Treasury*, XXXIV MICH. TAX L. 2, 20 (Spring 2008).

36. *Tyson Foods*, 276 Mich. App. at 691, 741 N.W.2d at 586 n.8.

37. *Id.*

38. *Id.* at 691, 741 N.W.2d at 586.

39. The author of this article must, under the practice of full disclosure, note that she was a member of Miller, Canfield, Paddock and Stone, PLLC, which had been counsel for the taxpayer at the time this matter was appealed to the court of appeals. However, while a member of Miller Canfield, she did not participate in the matter.

40. 277 Mich. App. 692, 746 N.W.2d 866 (2008).

interest is due on interest that the Department of Treasury ("the Department") was required to pay to the taxpayer.[41]

On leave granted from the court of claims, the court of appeals found that NSK Corporation (the "taxpayer") was entitled to interest on its overpayment of single business tax.[42] While the court of appeals affirmed the award of interest to the taxpayer on the amount of tax refunded, it remanded the matter back to the court of claims to determine the actual date from which such interest should accrue, which it found to be based upon when the Department became aware that a refund was due.[43] Additionally, the court of appeals differentiated between interest owed on the overpayment of tax from any statutory interest due (statutory interest had been awarded on the interest related to the overpayment of tax).[44] The court found that statutory interest *on interest* is only to be paid to taxpayers on interest payments that taxpayers have made to the Department on taxes that were "unjustly assessed, excessive in amount, or wrongfully collected."[45]

This matter arose from a single business tax audit of the taxpayer.[46] During the audit, the Department discovered that the taxpayer had overpaid its single business tax and was entitled to a refund.[47] The taxpayer received an audit determination letter informing it of this overpayment to which the taxpayer agreed.[48] The taxpayer asserted that it was entitled to interest on the overpayment pursuant to M.C.L. Section 205.30.[49]

On a motion for summary disposition before the court of claims, that court held that interest was due on the overpayment beginning forty-five days after the due date of the return for the applicable audit years.[50] Additionally, the court of claims granted the taxpayer additional statutory interest on the interest that the Department was ordered to pay, accruing

41. *Id.* at 696-98, 746 N.W.2d at 889-90.

42. *Id.* at 695, 746 N.W.2d at 888.

43. *Id.* at 697, 746 N.W.2d at 889.

44. *Id.* at 699, 746 N.W.2d at 890.

45. *Id.* at 698-99, 746 N.W.2d at 890 (citing MICH. COMP. LAWS ANN. § 205.30(1) (West 2003)).

46. *NSK Corp.*, 277 Mich. App. at 694, 746 N.W.2d at 887.

47. *Id.*

48. *Id.* at 694, 746 N.W.2d at 887-88.

49. *Id. See also* MICH. COMP. LAWS ANN. § 205.30(1) (mandating that interest be paid on all overpayment of taxes which are erroneously assessed and collected, unjustly assessed, excessive in amount, or wrongfully collected).

50. *NSK Corp.*, 277 Mich. App. at 694, 746 N.W.2d at 888.

from November 23, 2005, until paid in full.[51] It was from this decision that the Department appealed.[52]

The Department asserted that the taxpayer was not entitled to interest on its refunded overpayment because the taxpayer had never filed a claim to guarantee its right to interest if the Department did not refund the overpayment of tax within forty-five days of such claim.[53] Reviewing the specific language of M.C.L. Section 205.30,[54] the court of appeals noted, however, that the statute requires the Department to pay "interest at the rate calculated under Section 23 for deficiencies in tax payments" on any overpayments, and that such language does not make a refund contingent on the taxpayer discovering the overpayment and filing a claim.[55] Reiterating that the primary goal of statutory construction is to "ascertain and give effect to the intent of the Legislature,"[56] the court found that the language of the statute required the Department to pay interest on refunds of overpayments, regardless of whether it was the taxpayer or the Department that discovered the overpayment.[57] The court of appeals then turned to the issue of when such interest begins to run.[58]

The commencement of when interest begins to run is also addressed by M.C.L. Section 205.30, which provides that interest shall be added to a refund "commencing 45 days after the claim is filed or 45 days after the date established by law for the filing of the return, whichever is later."[59] The taxpayer took the position that because it did not file an actual claim for interest—having had such overpayment being discovered upon audit—interest began to accrue, by default, forty-five days after the return due date for each audit year.[60] Here, the court of appeals disagreed with the taxpayer's position.[61] The court of appeals noted that it had previously determined that for the purposes of M.C.L. Section 205.30, a claim is considered to be filed when the Department

51. *Id.*
52. *Id.*
53. *Id.* at 695, 746 N.W.2d at 888.
54. *Id.*
55. *Id.* at 695-96, 746 N.W.2d at 888-89.
56. *NSK Corp.*, 277 Mich. App. at 696, 746 N.W.2d at 889 (citing People v. Borchard-Ruhland, 460 Mich. 278, 284, 597 N.W.2d 1, 5 (1999)).
57. *Id.*
58. *Id.*
59. *Id.* at 695, 746 N.W.2d at 888 (citing MICH. COMP. LAWS ANN. § 205.30(3) (West 2003)).
60. *Id.* at 697, 746 N.W.2d at 889.
61. *Id.*

receives adequate notice of the claim.[62] As previously construed by the court in *Sager Trust*, the court held that the date on which the claim for interest would be treated as filed, would be the date on which the Department was made aware of the taxpayer's right to a refund.[63]

This date would be forty-five days after it conducted its audit and determined the taxpayer's overpayment. Therefore, interest should accrue starting forty-five days from the date of the Department's audit determination letter acknowledging the refund, which had been issued in March of 2005.[64] The court of appeals noted that to permit interest to accrue forty-five days after the date each return for the audit years at issue was filed would provide the taxpayer with an absurd windfall.[65] Allowing such a result would, in essence, reward a taxpayer for not taking steps to perhaps correct its own error, and punish the Department for bringing the error to the taxpayer's attention.[66]

The court of appeals also addressed whether additional statutory interest is due on the interest that the court of claims ordered the Department to pay to the taxpayer.[67] In reviewing the requirements of M.C.L. Section 205.30(1), the court of appeals concurred that when interest is paid, as defined in M.C.L. Section 205.30(1), a taxpayer is entitled to statutory interest on interest.[68] However, reading the subsection in context of the situation, the court noted that the statute requires that a payment of interest has been made by the taxpayer.[69] In the situation at hand, the taxpayer had not paid any interest; it had only overpaid its tax, and although entitled to interest on its overpayment, the court of appeals found that M.C.L. Section 205.30(1) does not entitle the taxpayer to additional statutory interest on any interest paid by the Department on the overpayment.[70]

The Michigan Supreme Court has denied leave to review.[71] However, in a twist of legal reasoning, the order issued by the Michigan Supreme Court stated that the Audit Determination Letter issued by the

62. *NSK Corp.*, 277 Mich. App. at 697, 746 N.W.2d at 889 (relying on Lindsay Anderson Sager Trust v. Dep't of Treasury, 204 Mich. App. 128, 132, 514 N.W.2d 514, 516 (1994)).

63. *Id.*

64. *Id.*

65. *Id.* at 697-98, 746 N.W.2d at 889-90.

66. *Id.*

67. *Id.* at 698, 746 N.W.2d at 890.

68. *NSK Corp.*, 277 Mich. App. at 699, 746 N.W.2d at 890.

69. *Id.* ("[T]he statute impl[ies] that a payment has been made.").

70. *Id.*

71. NSK Corp. v. Dep't of Treasury, 481 Mich. 884, 748 N.W.2d 884 (2008).

Department did not fully constitute a claim for refund.[72] The Michigan Supreme Court held that the taxpayer's April 26, 2005 letter to the Department was sufficient to constitute a claim for refund, and thus, interest on the overpayment would accrue forty-five days from that date.[73]

In looking at these results, practitioners should understand that although the decision is not particularly applicable to many other cases, it should not preclude further taxpayer claims for interest on a credit audit. Obviously, what will be paramount is documenting a right to a claim for refund immediately upon notice of an overpayment discovered by the Department in the course of an audit. Taxpayers and their practitioners should not wait until the issuance of a final audit determination letter before filing such claim for refund in order to fully obtain statutory interest to which they are entitled.

C. Wisne v. Michigan Department of Treasury

In reversing the imposition of discretionary penalties imposed by the Department of Treasury (the "Department"), the Michigan Court of Appeals[74] found that taxpayers could not be found liable for intentional disregard of the law, when such taxpayers relied on professional advice in taking a return position.[75] In addition, the court of appeals found that there was a distinction between intentional disregard of a law or rule, and the intentional disregard of instructions.[76]

The underlying assessment was for personal income taxes for the taxpayers' sale of their interest in a Subchapter S corporation during 1999.[77] The taxpayers had been Michigan residents up until March 31, 1999, and thereafter resided in Florida.[78] The sale of their business had concluded in 1999, and after consulting with their tax practitioner, they did not allocate a portion of the gain on the sale of their Subchapter S corporation to Michigan.[79] They paid only $100 in estimated taxes when they filed an extension of time to file their 1999 Michigan Income Tax

72. *Id.* at 884, 748 N.W.2d at 884.

73. *Id.* at 884-85, 748 N.W.2d at 884-85.

74. No. 270633, 2008 WL 2117136 (Mich. Ct. App. May 20, 2008).

75. *Id.* at *4.

76. *Id.* ("We see no reason why good-faith reliance on professional tax advice should not be considered in deciding whether a taxpayers' intentional disregard of *instructions* constituted an intentional disregard of the *law*.").

77. *Id.* at *1; *see also* MICH. COMP. LAWS ANN. § 206.301 *et seq.* (West 2003).

78. *Wisne*, 2008 WL 2117136, at *1.

79. *Id.*

return.[80] Upon the filing of their income tax return in October of 2007, they paid $2,416,950.00 due on the allocated gain of their interest in the Subchapter S corporation, having later determined that such allocation was appropriate.[81]

The Department assessed a penalty for failure to pay a sufficient amount of estimated tax due with the request for extension in the amount of $604,238.00.[82] This penalty is referred to as the "intentional disregard" penalty, and the imposition of such penalty is discretionary.[83] The taxpayers appealed the imposition of such penalty to the Michigan Tax Tribunal, which affirmed the penalty.[84] The taxpayers then appealed the penalty imposition to the court of appeals.[85]

The taxpayer's main defense was based on the premise that the intentional disregard penalty under the statute could not be sustained as there was no evidence that the taxpayers had the requisite intent to intentionally disregard the law as required by the statute.[86] The Department had relied on Revenue Administrative Bulletin (RAB) 1995-4, which provided that in regards to the imposition of the discretionary penalty, the taxpayer has the "burden of establishing facts, which will negate a finding of intent."[87] The Department had found that the taxpayer's reliance on tax professionals may be relevant to the reasonable cause defense to mandatory penalties, but is irrelevant as to the imposition of discretionary penalties for intentional disregard.[88]

The court of appeals found that the Department's decision should be overturned for several reasons.[89] First, the court of appeals stated that "[u]nlike the Single Business Tax Act . . . and the General Sales Tax Act . . . the Michigan Income Tax Act of 1967 does not declare that an assessment is prima facie correct and that the burden of proof is on the taxpayer."[90] The court of appeals found that the Department is not granted the authority to determine the burden of proof under the Michigan Income Tax Act.[91]

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80. *Id.*
81. *Id.*
82. *Id.*
83. *See* MICH. COMP. LAWS ANN. § 205.23(4) (West 2003).
84. *Wisne*, 2008 WL 2117136, at *1.
85. *Id.*
86. *Id.*
87. *Id.* (quoting Mich. Dep't of Treasury, Revenue Admin. Bulletin 1995-4, Penalty Provisions, at *8 (Mar. 30, 1995)).
88. *Id.* at *2.
89. *Id.*
90. *Wisne*, 2008 WL 2117136, at *2.
91. *Id.*

Second, the court of appeals found that there is a distinction between intentional disregard of a law or rule, and intentional disregard of instructions.[92] Reviewing the Department's reliance upon RAB 1995-4, the court once again reaffirmed its holding in *Catalina Marketing Sales Corporation v. Department of Treasury*[93] that Revenue Administrative Bulletin's are not promulgated under the Administrative Procedures Act,[94] are not considered administrative rules and do not have the force of law.[95] Indeed, RAB's are only "bulletins that explain the current department interpretations of current state tax laws."[96]

It was undisputed that the taxpayers correctly reported the income and paid the tax due in full, plus interest when they filed their actual return.[97] Therefore, the court of appeals found that there was no intentional disregard of the Department's instructions.[98] In noting the taxpayer's reliance upon professional advice received from practitioners, the court of appeals found that such reliance was pertinent and there was no evidence that the taxpayers, in any way, "misrepresented the facts to the tax professionals, or that they ignored admonitions that their position was contrary to a rule or law."[99] While statutory penalties were proper due to the late payment of tax, the Department's imposition of a twenty-five percent discretionary penalty for intentional disregard was in error.[100] The court noted that at the time the taxpayers filed the request for extension there was no promulgated rule or appellate precedence addressing the issue in the present case, although the same issue was presented to the court in 2001 in a matter involving a related party.[101]

The effect of *Wisne* may put a slight crimp in the Department of Treasury's actions of assessing as many penalties, both statutory and discretionary, that they can on any currently issued assessment. It is understood that the Department's current practice is driven by the need

92. *Id.* at *4.

93. 470 Mich. 13, 21, 678 N.W.2d 619, 624 (2004) (explaining that RAB's are not adopted under the Administrative Procedures Act, M.C.L. § 24.201 *et seq.*, and thus, do not have the force of law).

94. *See generally* MICH. COMP. LAWS ANN. §§ 24.201 *et seq.* (West 2004).

95. *Wisne*, 2008 WL 2117136, at *3.

96. *Id.* (citing *Catalina*, 270 Mich. 13, 21, 678 N.W.2d 619, 624 (2004)).

97. *Id.*

98. *Id.*

99. *Id.* at *4.

100. *Id.* at *5.

101. *See* Anthony Wisne v. Dep't of Treasury, 244 Mich. App. 342, 625 N.W.2d 401 (2001). A decision in this matter was not issued until after the petitioners in the instant case filed their request for extension.

for positive cash flow during our current fiscal crises.[102] Taxpayers are well advised to always submit a request for waiver of any discretionary penalties imposed prior to the close of an audit, if they suspect, which is likely, that such penalties will be imposed. If not, practitioners will find themselves challenging not only any additional tax which may be disputed, but also discretionary penalties to which there has not been the showing of the requisite intent needed by the Department to truly impose such penalties.

II. SALES, USE, EXCISE AND WITHHOLDING TAXES

A. Betten Auto Center v. Department of Treasury

In the long running dispute between the Michigan Department of Treasury (the "Department") and several automotive dealerships,[103] the Michigan Supreme Court finally put to bed the issue of whether or not demonstrator vehicles which dealerships purchase for resale were subject to use tax. In hearing oral arguments on applications for leave to appeal from an earlier 2006 judgment of the court of appeals,[104] the court affirmed the portion of the court of appeals holding that the demonstrating vehicles were exempt from use tax under the sale for resale exemption contained at M.C.L. Section 205.94(1)(c).[105] The Supreme Court vacated the balance of the judgment and held that a lower rate use tax would be due on demonstration vehicles that were in access of the permitted statutory number.[106]

This issue had been hotly contested by both the Department and the dealerships. In 2003, the Michigan Supreme Court, in an unpublished opinion, held that demonstrator vehicles purchased by licensed automobile dealerships were not subject to use tax, even though there may have been an intervening taxable use by employees of the dealership

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102. *See, e.g.*, Obama Makes Case as Bill Clears Hurdle, N.Y. TIMES, *available at* http://www.nytimes.com/2009/02/10/us/politics/10obama.html?_r=1 (last visited Apr. 21, 2009).

103. 478 Mich. 864, 731 N.W.2d 424 (2007) [hereinafter "*Betten II*"].

104. Betten Auto Center v. Dep't of Treasury, 272 Mich. App. 14, 723 N.W.2d 914 (2006) [hereinafter "*Betten I*"].

105. *Betten II*, 478 Mich. at 864, 731 N.W.2d at 424.

106. *Id.* The Supreme Court adopted the trial court's August 2, 2005 opinion and permitted the imposition of the 2.5 Demonstrator Vehicle Tax that is contained within M.C.L. Section 205.95(2). *Id.* This Section imposes a 2.5% use tax, plus $30 for each month the vehicle is used, for vehicles that are in excess of a dealers maximum allowable demonstration vehicles per year. MICH. COMP. LAWS ANN. § 205.95(2) (West 2009).

prior to the sale of the vehicles to the ultimate consumer.[107] Based on this unpublished opinion, Benton Auto Center, Inc., which included several affiliated automotive dealerships filed refund requests with the Department for approximately $48,449.74 in use taxes paid on demonstrator vehicles that were ultimately resold to consumers.[108] The Department denied the plaintiff's request for refund, asserting that *Crown Motors*, as an unpublished opinion, was not binding, and that use tax would be due on inventory that was used for other than demonstrated purposes.[109] The "other than for demonstration purposes" activities that the vehicles had been subject to, including allowing employees to use the vehicles after hours, which was limited to commuting purposes and other personal use which must be approved in advance by the dealership. The dealerships monitored the mileage of these demonstrator vehicles and ensured that the use of the vehicles would be kept to a minimum level.[110] The dealerships kept the use of each vehicle to approximately 5,000-6,000 miles per year. The vehicles maintained a window sticker listing the vehicle's features and pricings. Family members of the employees were not allowed to drive the vehicles, nor were the employees entitled to store any personal possessions in the vehicle. The employees could not smoke in the vehicle or drive the vehicles outside the normal selling area of the dealership. For this minimal usage, employees paid $25 per week to assist with insurance costs.[111] The Department believed that this intervening use by the employees prior to the ultimate sale of the demonstrator vehicle to the customer converted the vehicles purchased tax exempt with a sale for resale exemption to taxable vehicles. In addition, the Department argued that the believed that the lower 2.5% use tax rate imposed under M.C.L. Section 205.93(2) should apply to all plaintiff's vehicles.

The Michigan Supreme Court started with the basics, nothing that "*tax exemptions* are strictly construed against the taxpayer and in favor of the taxing authority."[112] As always, "because tax exemptions are disfavored, the taxpayer has the burden of proving entitlement to a tax exemption."[113] The Michigan Supreme Court dismissed the

107. *See* Crown Motors of Charlevoix, Ltd. v. Dep't of Treasury, No. 240555, 2003 WL 22495608 (Mich. Ct. App. Nov. 4, 2003).

108. *Betten I*, 272 Mich. App. at 15, 723 N.W.2d at 916.

109. *Id.* at 16, 723 N.W.2d at 917.

110. *Id.* at 16, 723 N.W.2d at 916.

111. *Id.*

112. *Id.* at 19, 723 N.W.2d at 918 (citing Nomads, Inc. v. Romulus, 154 Mich. App. 46, 55, 397 N.W.2d 210 (1986)) (emphasis in original).

113. *Id.* at 20, 723 N.W.2d at 918 (citing Elias Bros. Rests. Inc. v. Treasury Dep't, 452 Mich. 144, 150, 549 N.W.2d 837 (1996)).

Department's argument that the exempt vehicles had undergone a conversion to become non-exempt. The court noted that the fatal flaw in the Department's argument was that use tax is imposed on "consumer." The court did not find that the employees were consumers of the vehicles due to their limited use of the vehicles.[114] The court noted that although the term "consumer" is not defined in the taxing statute, that the definition of consumer in Black's Law Dictionary[115] would not consider the employees consumers of the vehicles.[116] The court did permit the Department's assessment of the lower rate 2.5% use tax (and accompanying $30 monthly charge) to apply to vehicles that exceeded the dealerships permitted allowance.[117]

Back and forth, back and forth, this case has gone until the taxpayer rightly received the result which had been awarded to them at the trial court level. Notwithstanding the granting to the Department of the lower tax rate for those demonstrator vehicles that exceeded the permitted usage, the case highlights the efforts to which the Department continues to boldly appeal whenever there has been a court awarded refund to a taxpayer. Indeed, as we have seen in recent times, another tool now used by the state to respond to court ordered refunds is simply to enact legislation prohibiting the payment of such refund.[118] The usefulness of this case is not in the specific effect to vehicle dealerships but in the message to all taxpayers that assist the state by collecting and remitting sales tax from the ultimate consumers and purchasers of the goods. One would think that the demonstrator vehicles in this case would appear to clearly be exempt from use and that the amount of tax at issue would not be worthy of such resistance by the Department to pay such refund. This resistance will likely continue, and in fact be exacerbated by the current economic climate. Some states—i.e. California—have already indicated that they will not and cannot pay out current year income tax refunds until the budget situation improves. This is in line with overall more legislation that retroactively prohibits the payment of refunds to

114. *Betten I*, 272 Mich. App. 22, 723 N.W.2d 919.

115. *Id.* The Court noted that if a statute does not define one of its terms, the Court was permitted to consult Black's Law Dictionary for guidance (citing Consumers Power Co. v Dep't of Treasury, 235 Mich. App. 380, 385, 597 N.W.2d 274 (1999)).

116. *Id.* at 22, 723 N.W.2d at 920.

117. *See* MICH. COMP. LAWS ANN. § 205.93(2) (West 2003).

118. *See* PA 105 of 2007, denying sales tax refunds for sales tax paid on vehicles repossessed or returned to dealerships.

taxpayers which had been court awarded. One should remember that a just government does not keep taxes to which it is not entitled.[119]

B. Ammex, Incorporated v. Department of Treasury

In a case of limited application, but with implicit result of interest to many practitioners,[120] the Michigan Court of Appeals upheld a refund of state motor fuel taxes finding that the federal scheme governing customs bonded warehouses preempted application of Michigan motor fuel tax to the sale of motor fuel by a duty free store.[121] The Michigan Department of Treasury (the "Department") appealed the finding of the court of claims entitling the taxpayer to a refund of state motor fuel taxes paid.[122] The case has a broad scope of application in that it allowed such refund to be applied retroactively, an event which taxpayers do not often experience.

In *Ammex*, (referred to by the court as "*Ammex II*") the taxpayer operated "a duty free store" in Detroit near the entrance to the Ambassador Bridge to Canada.[123] The duty free store is located upon private property, as are the surrounding streets and the Ambassador Bridge itself.[124] The actual duty free store is located in an area designated as "sterile" by the United States Custom Service.[125] During the tax

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119. Pittsburgh & Midway Coal Min. Co. v. Ariz. Dep't of Revenue, 776 P.2d 1061, 1065 (Ariz. 1989) ("An honorable government would not keep taxes to which it is not entitled . . . .").

120. 277 Mich. App. 13, 742 N.W.2d 617 (2007).

121. *Id.* at 22, 742 N.W.2d at 622. Note: there was no reliance by the court upon an earlier opinion that involves the same parties, also for a fuel tax related refund. *See generally* Ammex, Inc. v Dep't of Treasury, 237 Mich. App. 455, 603 N.W.2d 308 (1999).

122. *Ammex*, 277 Mich. App. at 15, 742 N.W.2d at 618. The taxes had originally been paid pursuant to the Michigan Motor Fuel Tax Act, which was subsequently repealed. *See* MICH. COMP. LAWS ANN. §§ 207.101 *et seq.* (West 2003), *repealed by* P.A. 2000, no. 403, § 169 (Apr. 1, 2001).

123. *Ammex*, 277 Mich. App. at 14, 742 N.W.2d at 618. These duty free stores are considered to be Class 9 United States customs bonded warehouses. *Id.* "Under federal law, a customs bonded warehouse is a building where imported goods may be stored, be manipulated, or undergo manufactured duty-free for a specific period." *Id.* n.2 (citing *Ammex II*, 272 Mich. App. at 288, 726 N.W.2d at 758 n.2); *see also generally* 19 U.S.C. §§ 1555, 1557.

124. *Ammex*, 277 Mich. App. at 14, 742 N.W.2d at 618.

125. *Id.* The designation "sterile" indicates that the physical design and operation of the facility guarantees the exportation of products sold therein. *Id.* n.4 (quoting Ammex, Inc. v. United States, 334 F. 3d 1052, 1054 (C.A.Fed. 2003)). To this extent, the store is considered to be "beyond the point of no return." *Ammex*, 277 Mich. App. at 14, 742 N.W.2d at 618. *See also id.* n.3. The phrase was used in the same context in related cases.

periods under review, the taxpayer sold gasoline and diesel fuel at the duty free store.[126] Ammex paid tax under the Michigan Motor Fuel Tax Act (MFTA) to its supplier when it purchased the fuel.[127] Upon the subsequent sale of the fuel to the final consumer, the taxpayer did not pass on the MFTA tax, but rather had applied for a refund of the taxes paid from the Department.[128] The court of claims ruled that the taxpayer was entitled to a refund, as the MFTA was unconstitutional under the Commerce Cause and Supremacy Cause of the U.S. Constitution.[129] Even if the tax was constitutional, the taxpayer would still be entitled to a refund, as it would have qualified under the non-highway use exemption of the MFTA.[130]

The court of claims concurred, finding that the MFTA was preempted by "the federal government's extensive statutory and regulatory scheme governing bonded warehouses and that the MFTA would be an obstacle to the full accomplishment and objectives of Congress."[131] In citing its prior decision, the court of appeals reiterated that "the state motor fuel tax and the state sales tax are preempted by the comprehensive federal regulation of customs bonded warehouses because 'the state law stands as an obstacle to the accomplishment and execution of the full objectives of Congress[.]'"[132]

The Department contended that *Ammex II* was not controlling, as during the tax periods at issue the United States Customs Service had not permitted the taxpayer to sell duty free gasoline and diesel fuel at its facility.[133] The Department maintained that the court of International

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Id. (citing Ammex, Inc. v. Dep't of Treasury, 273 Mich. App. 623, 732 N.W.2d 116 (2007), and *Ammex*, 334 F.3d 1052 (Fed. Cir. 2003)).

126. *Ammex*, 277 Mich. App. at 15, 742 N.W.2d at 618.

127. *Id.*

128. *Id.* The Department of Treasury refused to refund the taxes and the taxpayer filed complaints for the 1997 and 1998 tax periods which were consolidated for trial at the Court of Claims. The parties stipulated that the amount of tax at issue was $706,561.00. *Id.*

129. *Id. See also* U.S. CONST. art. I, § 8, cl. 3; U.S. CONST. art. VI, cl. 2.

130. *Ammex*, 277 Mich. App. at 15, 742 N.W.2d at 618; *see also* MICH. COMP. LAWS ANN. § 207.122 (repealed 2001).

131. *Ammex*, 277 Mich. App. at 17, 742 N.W.2d at 619 (citing *Ammex II*, 272 Mich. App. at 497, 726 N.W.2d at 763 (quoting Lavene v. Winnebago Indus., 266 Mich. App. 470, 479, 702 N.W.2d 652, 657 (2005))).

132. *Id.*

133. *Id.* at 18, 742 N.W.2d at 620. This action by the United States Custom Service had forced an opinion from the United States Court of International Trade (CIT), which was issued on August 25, 2000 and held that the Customs Services refusal was contrary to 19 U.S.C. 1557(a)(1). *Id.*

Trade's (CIT) decision could not apply retroactively to allow Ammex a motor fuel tax act refund.[134]

The Michigan Court of Appeals found the Department's position to be untenantable.[135] The court of appeals held that the CIT's decision must be given retroactive application, as the CIT's decision merely applied the law as it was written and did not announce a new rule of law.[136] As the Department stipulated that the taxpayer had sold the fuel tax free, the court of appeals found that the taxpayer was entitled to a refund of the tax that it had paid.[137]

C. Infusystem, Inc. v. Michigan Department of Treasury

In a final opinion and judgment granting the Petitioner's motion for summary judgment,[138] the Michigan Tax Tribunal held that a chemotherapy infusion pump qualifies for exemption from sales and use tax as a medical device used to assist a disabled person to lead a reasonably normally life.[139] The importance of this decision is not in the holding of the Michigan Tax Tribunal but is included in this volume to illustrate the absolutely absurd level of conduct to which the Michigan Department of Treasury (the "Department") has risen in its seemingly unending quest for the narrowest interpretation of laws which were passed to reduce the tax burden on Michigan citizens. In order to maintain a level of professional objectivity within this publication, a brief review of the facts is required.

The Petitioner, Infusystem, Inc., is engaged in providing portable infusion pumps to those who suffer from advanced stages of cancer.[140] It is necessary to receive a prescription in order to obtain such device which allows patients to receive chemotherapy treatment while not being confined to a bed or medical facility.[141] For the period from February 1, 1989 through September 1, 2004, Petitioner did not collect sales tax upon its sale of such devices nor did it remit use tax, relying upon the exemption for medical devices under the statute at the time.[142] In

134. *Id.*

135. *Id.*

136. *Id.* at 21, 742 N.W.2d at 621 (citing Lindsey v. Harper Hosp., 455 Mich. 56, 68-9, 564 N.W.2d 861, 867 (1997)).

137. *Ammex*, 277 Mich. App. at 21-22, 742 N.W.2d at 622.

138. 2007 Mich. Tax. LEXIS 15 (Apr. 24, 2007).

139. *Id.* at *8.

140. *Id.* at *3.

141. *Id.*

142. *Id. See also* MICH. COMP. LAWS ANN. § 205.94(r) (West 1978) (amended 2004) (providing an exemption for medical devices that assist disabled persons in leading a

conducting their audit, the Department determined that the infusion pumps did not qualify for the exemption from sales or use tax, and issued an assessment in the amount of $263,748.00 plus $53,177.00 in interest.[143] Petitioner requested an informal conference, which resulted in a reversal of the assessment based on the hearing referee's proposed decision.[144] However, the Department did not agree with the hearing referee's proposed decision, and issued a decision and order of determination upholding the assessment.[145] The taxpayer filed its case before the Michigan Tax Tribunal.[146] While both parties agreed that the infusion pump was a medical device, the issue before the Michigan Tax Tribunal was whether the infusion pump was the type of device that the legislature intended to qualify for the exemption.[147] Specifically, as the language of the exemption was written at the time, the question was whether the pump was used to replace or substitute any part of the human body, or if it was used to assist a disabled person leading a reasonably normal life.[148]

The absurdity of the Department's arguments made at the tax tribunal hearing ranged from (1) that cancer patients do not qualify as disabled persons, to (2) that the devices do not help cancer patients lead a reasonably normal life.[149] The Department actually alleged that a person is only disabled if "missing a body part or having a body part that does not perform its function properly and there is a corresponding disabled or diminished body function."[150] The Department also argued that infusion pumps offer only "convenience to individuals who need to take medicines" and that "[a] person is not leading a reasonably normal life if that person is prolonging life."[151] The Michigan Tax Tribunal, while noting that it did not completely disagree with the Department's position of what is meant by a "reasonably normal life," disagreed with the argument that prolonging life is contrary to leading a normal life.[152] The Michigan Tax Tribunal found that "a long and healthy life is the goal of a

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"reasonably normal life"). The taxpayer had not paid use tax, relying on a 1989 letter issued by the Department that allowed such exemption for the devices. *Infusystem*, 2007 Mich. Tax LEXIS 15, at *2.

143. *Infusystem*, 2007 Mich. Tax LEXIS 15, at *3. It should be noted that this works out to be a little over $63,000 per audit year in additional revenue to the state.

144. *Id.* at *4.

145. *Id.*

146. *Id.*

147. *Id.*

148. *Id.*

149. *Infusystem*, 2007 Mich. Tax LEXIS 15, at *2-3.

150. *Id.* at *9.

151. *Id.* at *11-12.

152. *Id.* at *11-12.

reasonably normal life," and that, "to set a standard" requiring a device to meet such standard, would be "counterintuitive and demeaning."[153]

What is demeaning to this author is the magnitude of resources wasted on issuing an assessment, overruling the hearing officer's proposed decision, and failing to settle this matter prior to an actual hearing; also demeaning is the amount of time and effort expended by the Attorney General's office to defend such matter, and the requirement that cancer patients attend such hearing so that they may demonstrate, via evidentiary submission, that a portable infusion pump provides an ability to lead a "normal life." In an attempt to collect less than $300,000 in taxes, it must be noted that significant state resources were expended in pursuing this matter by the Department, including the use of limited Assistant Attorney General efforts to persecute this matter (and all paid for by the taxpayers of this State).[154] The audacity of the Department to chase after such amounts is astounding. There is so much press at both the state and national level about the enormous "tax gap" which represents the amount of unpaid or underpaid taxes from those who deliberately defraud the state treasuries of those levies which are legally imposed upon them.[155] One would think that the Department would have a much more prioritized set of audit criteria to better focus their efforts. It must be highlighted that any sales or use tax due upon these devices would, in the end, be borne by the actual patients themselves when they went to their local pharmacy or medical supply center to pick up such device. This case should stand not for the ability of the Michigan Tax Tribunal to uphold the law and make the right decision, but on the audacity of the Department to continue to pursue such matters, after a dismissal by a professional and competent hearing officer.

D. WMS Gaming Inc. v Department of Treasury

In *WMS Gaming*,[156] the Michigan Court of Appeals addressed the issue of whether a manufacturer of gaming equipment may elect to pay sales tax on the price of the components used to produce the equipment which are later leased, or pay use tax on the stream of rental receipts from the lease of such machines.[157] The general rule in Michigan is that a

153. *Id.* at *13-14.

154. *Id.*

155. Urban Institute No. 13, April 8, 2008, *available at* www.urban.org/decision-points08/archive/13taxgap.cfm (last visited Apr. 20, 2009).

156. 274 Mich. App. 440, 733 N.W.2d 97 (2007). It should be noted that members of the author's firm represented the plaintiff in this matter.

157. *Id.* at 441, 733 N.W.2d at 97.

lessor may either pay sales or use tax at the time it purchases an item which will be leased, or it may collect sales tax on the stream of rental receipts.[158] The twist in the general rule before the court was whether WMS Gaming, as both the manufacturer and the lessor, could make such election, and, if such election was permitted, if sales tax would be due solely on the cost of the components parts or if the manufacturer must also include its cost of labor and overhead allocated to the product within the tax base.[159]

The taxpayer was a Delaware corporation that had its principle offices in the state of Illinois.[160] The taxpayer manufactured gaming equipment which is used in casino gambling.[161] The manufacturing process occurred entirely in Illinois.[162] Upon production of the equipment the taxpayer either sold or leased the equipment to its customers.[163] Three Michigan casinos chose to lease gaming equipment produced by the taxpayer.[164] This matter arose from a claim for refund for use tax paid by the taxpayer under protest from assessments issued by the Michigan Department of Treasury ("the Department").[165] The Department had subjected the equipment to use tax based upon the rental receipts received by the taxpayer.[166] The taxpayer claimed that it had the option to pay use tax calculated on the cost of the components used to produce the equipment, rather than being forced to pay use tax on the rental receipts from the Michigan casinos.[167]

While the court of claims had granted the Department's motion for summary disposition,[168] concluding that to impose use tax on the cost of the raw materials used out-of-state in the manufacturing process would essentially be "imposing a tax on purchases that occurred outside the state of Michigan,"[169] the court of appeals reversed, finding such decision to have been made in the error.[170] The court of appeals explained that use tax is complimentary to the sales tax, and it is properly

158. *See* MICH. ADMIN. CODE R. 205.132(1) (1999).

159. *WMS Gaming*, 274 Mich. App. at 445-46, 733 N.W.2d at 100. This issue has been reviewed in numerous other states but, as of the time of *WMS Gaming*, had not yet been the primary issue in a Michigan case.

160. *Id.* at 441, 733 N.W.2d at 97.

161. *Id.*

162. *Id.*

163. *Id.*

164. *Id.*

165. *WMS Gaming*, 274 Mich. App. at 441, 733 N.W.2d at 97.

166. *Id.*

167. *Id.* at 441-42, 733 N.W.2d at 97.

168. *Id.* at 442, 733 N.W.2d at 98.

169. *Id.* at 442, 733 N.W.2d at 99.

170. *Id.*

imposed on property that is purchased out of state and brought into Michigan for use within the state.[171] The court noted that "[it] has long been held that the tax on the use of imported goods is not a tax on out of state sales even if that tax is based on the purchase price in the other state."[172]

The Department acknowledged that there were two methods of calculating the sales and used tax with regard to rental equipment.[173] However, the Department had relied upon its interpretation that a manufacturer who leases property that it has self-manufactured cannot be considered to be a "lessor-consumer" as it would not have "purchased" the tangible personal property that they then provided for lease.[174] The court of appeals looked to its holding in *International Business Machines v. Department of Treasury*,[175] which held that the calculation of use tax owed by the plaintiff on computers that it had self manufactured, but consumed in the course of its own business, should be calculated upon the cost of the raw materials and components parts used in the manufacturer of the computers.[176] In holding for the taxpayer in *International Business Machines*, the court of appeals looked to the

171. *WMS Gaming*, 274 Mich. App. at 443, 733 N.W.2d at 99 ("It is the use in Michigan that is taxed under the use tax, precisely because it is not subject to the sales tax.").

172. *Id.* (noting generally Henneford v. Silas Mason Co. Inc., 300 U.S. 577 (1937)).

173. *WMS Gaming*, 274 Mich. App. at 444, 733 N.W.2d at 100; *see also* MICH. ADMIN. CODE R. 205.132(1) (1999). The Administrative Code provides:

> a person engaged in the business of renting or leasing tangible personal property to others shall pay the Michigan sales or use tax at the time he purchases tangible personal property, or he may report and pay use tax on the rental receipts from the rental thereof. A person remitting tax on the purchase price as a purchaser– consumer on remitting tax or rental receipts as a lessor, shall follow 1 or the other methods of remitting for his entire business operation.

Id.

174. *WMS Gaming*, 274 Mich. App. at 445, 733 N.W.2d at 100. The Department's interpretation was based off of the Michigan Department of Treasury's Revenue Administrative Bulletin (RAB) 1988-39. Michigan Department of Treasury, Revenue Administrative Bulletin 1988-39, Sales and Use Taxes-Lessors (June 10, 2988), *available at* http://www.michigan.gov/treasury/1,1607,7-121-1748_1904_2027-7357--,00.html (last visited Apr. 20, 2009). This RAB established the categories of lessor-consumer and lessor-retailer. A lessor-consumer is considered to be a lessor who pays sales tax on the purchase price of the property which has been leased, and thus, the rental receipts are not subject to use tax. A lessor-retailer is considered to be a lessor who does not pay sales tax on the purchase of the property but who later pays use tax on the stream of rental receipts. *Id.*

175. 220 Mich. App. 83. 558 N.W.2d 456 (1996).

176. *Id.* at 84, 558 N.W.2d at 456.

definition of "price" under M.C.L. Section 205.92(f)[177] and agreed that "price," for purposes of self-manufactured goods, is based upon the material costs, not the total value of the finished product,[178] whereas the Department had taken the position that use tax should be on the total manufactured cost of the equipment—which would include both labor and overhead costs, as well as that of the raw materials.[179] The court of appeals noted that the out-of-state origins of the equipment have no bearing at all on the ability of the lessor to make the use tax election, and characterized such argument by the Department as a "red herring."[180] Notably, the court also granted the taxpayer costs in the matter.[181] This firmly highlights the rights of the lessors to make the use of tax election as permitted by statute, while also reminding the Department that taxpayer's are not entitled to be reimbursed for their efforts not to pay, but for taxes which were frivolously assessed.

III. AD VALOREM TAXES

A. Kinder Morgan Michigan, LLC v. City of Jackson

In a matter before the Michigan Court of Appeals to determine whether or not a taxpayer's renaissance zone property was exempt from taxes levied to support the local community's pension system for firefighters and police officers,[182] the court determined that pension obligations of local taxing jurisdictions are not obligations that pledge the unlimited taxing power of the local government unit.[183] Since such obligations do not pledge the unlimited taxing power of the local government, the court determined that taxes to fulfill such obligations cannot be levied on qualified renaissance zone property.[184] More importantly, the court's decision provides a clear limitation to the state tax commission's seemingly unfettered discretion to administer the law under the General Property Tax Act.[185]

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177. *See* MICH. COMP. LAWS ANN. § 205.92(f) (West Supp. 2007).
178. *WMS Gaming*, 274 Mich. App. at 445-46, 733 N.W.2d at 100.
179. *Id.*
180. *Id.* at 447, 733 N.W.2d at 101.
181. *Id.*
182. 277 Mich. App. 159, 744 N.W.2d 184 (2008).
183. *Id.* at 169-72, 744 N.W.2d at 191-92.
184. *Id.* at 172, 744 N.W.2d at 192.
185. *Id.* at 173, 744 N.W.2d at 193 ("[T]he Tax Tribunal properly declined to defer to the State Tax Commission's contrary interpretation of the statute."); *see also id.* at 193 n.3 (explaining that the commission's property tax division was not a properly promulgated administrative rule, and therefore, did not have the force of law).

The case at issue was straight forward. In a pair of consolidated cases, the taxpayers individually owned real and personal property within the City of Jackson.[186] The property was situated in a renaissance zone, which had been properly established pursuant to Michigan's Renaissance Zone Act.[187] The city levied a property tax that was dedicated to funding its pension system for firefighters and police officers (the "Pension Tax").[188] The city had established its pension system several years prior to the tax years at issue, but had never levied the pension taxes on property located in a renaissance zone.[189] In 2004, the city received a letter from the State Tax Commission's property tax division that had instructed the city that the pension taxes should be collected from all properties, including renaissance zone properties.[190] Following this guidance, the city subsequently began to levy the pension taxes against the taxpayer's real and personal property located in the renaissance zone.[191]

The taxpayers became aware of such levy when they received their summer 2005 tax bills, and protested the levy before the July board of review.[192] Finding that there had been no clerical errors or mutual mistake of fact, the board of review denied the taxpayers' request to remove the levy from their tax bills.[193] The taxpayers appealed to the Michigan Tax Tribunal.[194] At the tax tribunal, the taxpayers contended that only those property taxes specifically enumerated in the General Property Tax Act could be levied against renaissance zoned property.[195]

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186. *Id.* at 161, 744 N.W.2d at 187.

187. *Kinder Morgan*, 277 Mich. App. at 161, 744 N.W.2d at 187; *see also generally* MICH. COMP. LAWS ANN. §§ 125.2681 *et seq.* (West 1996).

188. *Kinder Morgan*, 277 Mich. App. at 161, 744 N.W.2d at 187. The city was authorized to impose such levy pursuant to the Firefighters and Police Officers Retirement Act. *See* MICH. COMP. LAWS ANN. §§ 38.551 *et seq.* (West 2005).

189. *Kinder Morgan*, 277 Mich. App. at 161, 744 N.W.2d at 187.

190. *Id.* at 162, 744 N.W.2d at 187. The letter from the State Tax Commission's property tax division provided that "the following is a list of what should be levied on qualified Renaissance Zone property. Please make sure you are levying the appropriate millage . . . . Any obligations pledging the unlimited taxing power of the local unit such as Court Ordered Judgments [*sic*] or Pension [Taxes]." *Id.* at 161-62, 744 N.W.2d at 187.

191. *Id.* at 162, 744 N.W.2d at 187.

192. *Id.*

193. *Id.* Note: under the authority of the General Property Tax Act, Act 206 of 1893, as amended, local boards of review are only able to make changes if there are clerical errors or mutual mistakes of fact. *See* MICH. COMP. LAWS ANN. § 211.29 (West 2007).

194. *Kinder Morgan*, 277 Mich. App. at 162, 744 N.W.2d at 187.

195. *Id.* The General Property Tax Act provides in relevant part:

> Real and personal property in a renaissance zone is not exempt from collection of the following: (a) A special assessment levied by the local tax collecting unit in which the property is located. (b) Ad valorem property taxes specifically

The issue decided at the Tax Tribunal was whether or not the Pension Taxes fit into the category as provided in M.C.L. Section 211.7ff(2)(b) that "[a]d valorem property taxes specifically levied for the payment of principle and interest of obligations . . . pledging the unlimited taxing power of the local government unit."[196] The Michigan Tax Tribunal granted the taxpayers' motion for summary disposition and found that pension taxes did not fall within the scope of the taxes described in M.C.L. Section 211.7ff(2)(b), and therefore, could be levied on renaissance zone property.[197] The Michigan Tax Tribunal noted that it was not bound by the State Tax Commission's contrary interpretation of the statute.[198]

The court of appeals began its analysis by fully acknowledging that while tax exemption statutes must generally be narrowly construed in favor of the taxing authority, such statutory interpretation does not "permit a strained construction adverse to a Legislature's intent."[199] In reviewing the legislature's intent in establishing renaissance zones, the court of appeals noted that the legislature expressly set forth the purposes of the Renaissance Zone Act and had decreed that such Act "shall be construed liberally to effectuate the legislative intent and the purposes of this act," and that "all powers granted by this act shall be broadly interpreted to effectuate the intent and purposes of this act and not as a limitation of powers."[200]

> levied for the payment of principle and interest of obligations approved by the electors or obligations pledging the unlimited taxing power of the local government unit. (c) A tax levied under section 705, 1211c, or 1212 of the revised school code, 1976 PA 451, MCL § 380.705, 380.1211c, and 380.1212.

MICH. COMP. LAWS ANN. § 211.7ff(2) (West 2005).

196. *Kinder Morgan*, 277 Mich. App. at 162, 744 N.W.2d at 187; *see also* MICH. COMP. LAWS ANN. § 211.7ff(2) (West 2005).

197. *Kinder Morgan*, 277 Mich. App. at 162, 744 N.W.2d at 187.

198. *Id.* at 162, 744 N.W.2d at 188.

199. *Id.* at 165, 744 N.W.2d at 189 (citing Wexford Med. Group v. City of Cadillac, 474 Mich. 192, 204, 713 N.W.2d 734, 740 (2006); Nat'l Ctr. For Mfg. Sciences, Inc., v. City of Ann Arbor, 221 Mich. App. 541, 546 N.W.2d 65, 67 (1997)).

200. *Id. See also* MICH. COMP. LAWS ANN. § 125.2694 (West 2006) (identifying the rule of construction with regard to the Act). The legislature has also expressly identified the purpose of the Renaissance Zone Act:

> The legislature of this state finds and declares that there exists in this state continuing need for programs to assist certain local governmental units in encouraging economic development, the consequent job creation and retention, and ancillary economic growth in this state. To achieve these purposes, it is necessary to assist and encourage the creation of renaissance zones and provide temporary relief from certain taxes within the renaissance zones.

MICH. COMP. LAWS ANN. § 125.2682 (West 2006).

The court also noted that it was clear from the statutory language that the intent of the legislature was to grant significant tax relief for businesses located and conducting business activities in renaissance zones.[201] Given the broad interpretation of the Act, the court found that the general rule requiring narrow construction of tax exemptions does not apply in the context of the Renaissance Zone Act,[202] and adopted the taxpayers' reasoning that property taxes levied to support pension taxes are not a debt of the local jurisdiction and do not fall within the position of M.C.L. Section 211.7ff(2)(b).[203]

The court determined that such taxes constitute a general operating expense of the municipality.[204] As a general operating expense of the municipality, such pension taxes are not "obligations pledging the unlimiting taxing power of the local government unit,"[205] nor are such taxes "specifically levied for the payment of principle and interest."[206] The court further concluded that while the pension taxes themselves were obligations of the local unit of government, they were not debt obligations, and instead represented that "an accrued liability or general operating expense of the local unit of government."[207] What makes this case noteworthy is the extent to which the Michigan Court of Appeals, after reaching its finding, emphasized in dicta the Michigan Tax Tribunal's proper actions in declining to defer to the state tax commission's contrary interpretation of the General Property Tax Act.[208]

The court cited numerous prior decisions to reiterate that while the "Court generally defers 'to the Tax Tribunal's interpretation of a statute that it is charged with administering and enforcing,'"[209] a longstanding administrative interpretation cannot overcome the intent of the Legislature.[210] The court also pointed out that the 2004 letter from the State Tax Commission's property tax division was not a properly promulgated administrative rule, and therefore, did not have the force of

201. *Kinder Morgan*, 277 Mich. App. at 165-66, 744 N.W.2d at 189.
202. *Id.* at 166, 744 N.W.2d at 189.
203. *Id.* at 169, 744 N.W.2d at 191 n.2.
204. *Id.*
205. *Id.*
206. *Id.* at 169, 744 N.W.2d at 191 n.2.
207. *Kinder Morgan*, 277 Mich. App. at 172, 744 N.W.2d at 192.
208. *Id.* at 173, 744 N.W.2d at 193.
209. *Id.* at 171, 744 N.W.2d at 192 (citing 20th Century Fox Home Entm't Inc. v. Dep't of Treasury, 270 Mich. App. 539, 548, 716 N.W.2d 598, 603 (2006) (quoting Michigan Milk Producers Ass'n. v Dep't of Treasury, 242 Mich. App. 486, 491, 618 N.W.2d 917 (2000))).
210. *Id.* at 173, 744 N.W.2d at 193 (citing Howard Pore, Inc. v State Comm'r of Revenue, 322 Mich. 49, 33 N.W.2d 657 (1948); Buttleman v. State Employees' Ret. Sys., 178 Mich. App. 688, 444 N.W.2d 538 (1989)).

law.[211] Many practitioners have seen an increase in guidance sent out by the state tax commission under the misguided belief that their mere communications have the force of law, and should be strictly adhered to by all local assessors.[212]

We are in unprecedented times with a previously never before seen number of cases before the state tax commission and the tax tribunal regarding issues of valuation and classification. Rather than working with the practitioner community and the administration to resolve issues of interpretation, the State Tax Commission has taken it upon themselves to provide a manifest destiny of guidance, in which unclear and often inconsistent guidance is spued forth to be followed by the local assessors. There is no legal precedence for this guidance, and many taxpayers are unaware that there is no avenue of appeal to the one-sided determinations being issued by the state tax commission. Any decision made by the State Tax Commission cannot be appealed to the circuit courts in Michigan, nor to the court of appeals or Supreme Court of the state. This mockery of due process should be at the top of those issues to be reviewed by the administration in its new term in order to provide the citizens of Michigan a fair and equitable legal system to voice their protests. One doubts that the State Tax Commission will take heed of decisions such as *Kinder Morgan* and adjust their behavior accordingly.

B. Toll Northville Ltd. v. Township of Northville

In a case of first impression,[213] the Michigan Supreme Court, held that public service improvements do not constitute taxable "additions" under the Michigan Constitution and General Property Tax Act, as title to the improvements will ultimately vest in a municipality or utility company, and that the increase in taxable value attributable to such additions is most appropriately taxed upon the completion of the sites to which such public utility services will serve.[214]

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211. *Kinder Morgan*, 277 Mich. App. at 173, 744 N.W.2d at 193 n.3 (citing Danse Corp. v. City of Madison Heights, 466 Mich. 175, 181, 644 N.W.2d 721, 725 (2002)).

212. This guidance can take the form of a publication, memorandums, issued correspondence, directions or bulletins, as the State Tax Commission themselves deem necessary. To understand the tone and nature of the guidance, as well as the breadth of knowledge to which the commission deems themselves to be the final judge and jury, readers are urge to visit the State Tax Commission's website which can be viewed at www.michigan.gov/treasury/0,1607,7-121-1751_2228---,00.html (last visited Apr. 20, 2009).

213. 480 Mich. 6, 743 N.W.2d 902 (2008).

214. *Id.* at 10, 15, 743 N.W.2d at 905, 908; *see generally* MICH. CONST. art. 9, §31 (excluding the value of the new construction and improvements); *see also* MICH. COMP. LAWS ANN. § 211.34(d)(1)(b)(viii) (West 2005).

At issue was whether the definition of "additions," which was defined both in the Michigan Constitution[215] as well as within the Michigan General Property Tax Act,[216] is inconsistent, and whether taxing public service improvements under both definitions would result in double taxation.[217] The Michigan Supreme Court affirmed, in part, the judgment of the court of appeals which held that M.C.L. Section 211.34(d)(1)(b)(viii) was unconstitutional as it was inconsistent with the meaning of "additions" used in the Michigan Constitution.[218] The taxpayers were real property developers who had invested significant sums to install infrastructure services for condominium and single family residential lots located in Northville Township.[219] The infrastructure was required to be put in place before the developers could receive final plat approval for the proposed subdivision.[220] Relying on the definition of "additions" contained in the General Property Tax Act, Northville Township increased the value of the taxpayers' real property, and subsequently the related tax assessment, by including the enhanced value resulting from the public service improvements in the value of the real property.[221]

The taxpayers challenged the assessment to the Michigan Tax Tribunal claiming that such valuation increases violated the Michigan Constitution.[222] This appeal was stayed by the Michigan Tax Tribunal "so that [a] declaratory action regarding the constitutionality of the statute could proceed in circuit court."[223] The circuit court held that M.C.L. Section 211.34(d)(1)(b)(viii) was unconstitutional because it taxed the improvements to real property beyond the meaning of "additions" as used in the constitution.[224] The court of appeals affirmed the circuit court's judgment on the declaratory action, and also found that the taxpayers would not owe property tax on these improvements, as the tax would become due once title to the improvements ultimately vested

215. *See* MICH. CONST. art. 9, § 3 (amended 1994).

216. *See* MICH. COMP. LAWS ANN. § 211.34(d)(1)(b)(viii) (West 2005).

217. *Toll Northville*, 480 Mich. at 8-9, 743 N.W.2d at 904.

218. *Id.*

219. *Id.* at 9, 743 N.W.2d at 904. The infrastructure consisted of primary access roads, streetlights, sewer service, water service, electrical service, natural gas service, telephone service, and sidewalks. *Id.*

220. *Id.*

221. *Id.* at 9, 743 N.W.2d at 904-05.

222. *Id.* at 9, 743 N.W.2d at 905. Specifically the taxpayers claims that such increase violated Article 9, Section 3 of Michigan's Constitution.

223. *Toll Northville*, 480 Mich. at 9, 743 N.W.2d at 905.

224. *Id.* at 9-10, 743 N.W.2d at 905.

in the municipality or utility company.[225] The township appealed this finding to the Michigan Supreme Court, and the Supreme Court reached finality on the issue regarding the constitutionality of M.C.L. Section 211.34(d)(1)(b)(viii) and whether public service improvements constitute an "addition" under the statute.[226]

The Michigan Supreme Court upheld the court of appeals' ruling that concluded that the installation of public service improvements on public property or utility easements, does not constitute a taxable "addition," as that term was contemplated in the adoption of Proposal A under the Constitution.[227] Proposal A was adopted to limit increases in property taxes as long as the property remained owned by the same party.[228] Proposal A provided such limitation by capping the amount that the "taxable value" of the property could increase each year, even if the "true cash value" rose at a greater rate.[229] However, Proposal A contained an exception to allow for adjustments due to "additions." At the time Proposal A was adopted, the General Property Tax Act defined "additions" as "improvements caused by new construction."[230] However, after the adoption of Proposal A, the legislature amended the definition

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225. *Id.* at 10, 743 N.W.2d at 905. M.C.L. § 211.34(d)(1)(b)(viii) provides that "for taxes levied after 1994," "additions" means, except as provided in subdivision (c), all of the following:

> Public services. As used in this subparagraph, "public services" means water service, sewer service, a primary access road, natural gas service, electrical service, telephone service, sidewalks, or street lighting. For purposes of determining the taxable value of real property under section 27a, the value of public services is the amount of increase in true cash value of the property attributable to the available public services multiplied by 0.50 and shall be added in the calendar year following the calendar year when those public services are initially available.

MICH. COMP. LAWS ANN. § 211.34(d)(1)(b)(viii) (West 2005).

226. Toll Northville, Ltd. v Northville Twp., 272 Mich. App. 352, 375, 726 N.W.2d 51 (2006).

227. *Toll Northville*, 480 Mich. at 16, 743 N.W.2d at 908. Proposal A amended Article 9, § 3 of the Michigan Constitution in 1994. Proposal A provided:

> [f]or taxes levied in 1995 and each year thereafter, the legislature shall provide that the taxable value of each parcel of property adjusted for additions and losses, shall not increase each year by more than the increase in the immediately preceding year in the general price level, as defined in section 33 of this article, or 5 percent, whichever is less until ownership of the parcel of property is transferred.

Id. at 11-12, 743 N.W.2d at 906.

228. *Id.* at 12, 743 N.W.2d at 906.

229. *Id.* True cash value reflects the actual market value of the property (citing WPW Acquisition Co v. City of Troy, 466 Mich. 117, 112, 643 N.W.2d 564, 567 (2002)).

230. *Id.* at 12-13, 743 N.W.2d at 906 (citing WPW Acquisition at 122, 643 N.W.2d at 567 (quoting MICH. COMP. LAWS ANN. § 211.34(d)(1)(a) (West 2005))).

of "additions" to be "all increases in value caused by new construction or a physical addition of equipment or furnishings."[231] This amendment eliminated any reference to "improvements caused by new construction."[232] The Michigan Supreme Court determined that the later amendment to Proposal A superseded the prior General Property Tax Act definition of the term "additions."[233] In doing so, the Michigan Supreme Court properly aligned the term "additions" as used in the Michigan Constitution with the interpretation of the same term General Property Tax Act, and concluded that public service improvements do not constitute "additions" to property within the meaning of Proposal A.[234]

The Court dismissed the township's agreement that the definition of "additions" as provided in the Headlee Amendment should be found to be controlling.[235] The Headlee Amendment was adopted in 1978 to limit changes in the tax base by placing an inflation rate cap on the increase in taxes on the local taxing authorities in regard to all property contained within a local union of government.[236] The Court found that amendments of Proposal A contained in 1993 P.A. 145, which eliminated the phrase "improvements caused by new construction," superseded the definition of additions contained within the Headlee Amendment.[237]

In finally deciding this issue, the Court has effectively saved taxpayers thousands of dollars by definitively determining an issue that has consistently been before the Michigan Tax Tribunal. Holdings of such clarity, which clearly resolve any contestant ambiguity that may be raised by a claimant in bringing or defending such actions, are to be applauded. This does not mean that Northville Township has lost out on any increases in value that has occurred within their jurisdictional boundaries. The "additions" at issue were not located on the actual real property parcels affected. Any increase in value due to these improvements could only increase assessed value, and could not be used to increase taxable value until the property changed hands and there was an uncapping under Proposal A. Indeed, as the court pointed out in the majority opinion, the value due to the additions of the availability of utility services will be incorporated into and taxed on the value of each

231. *Id.* at 13, 743 N.W.2d at 906.

232. *Id.*

233. *Toll Northville*, 480 Mich. at 15, 743 N.W.2d 907-08.

234. *Id.* at 16, 743 N.W.2d at 908.

235. *Id.* at 14, 743 N.W.2d at 907.

236. *Id. See also* MICH. CONST. art. 9, § 31. The Headlee Amendment, defined additions as "all increases in value caused by new construction, improvements caused by new construction or a physical addition of equipment or furnishings . . . ." MICH. COMP. LAWS ANN. § 211.34(d)(1)(a) (West 2005).

237. *Toll Northville*, 480 Mich. at 15, 743 N.W.2d at 907.

individual home at the time it is built or sold at the development site.[238] Thus, the issue here was really one of timing, not of whether or not such value would be taxed at all. Given the current real estate market in Michigan, and the Detroit area in particular, there is no doubt that the township was more eager to obtain an increase in value from the developer directly, rather than waiting until construction was complete, or until the property was sold to the ultimate buyer. While one must be sympathetic to the plight of local jurisdictions in these times of decreasing property values and resultant decrease on local revenues, the law must be followed.

238. *Id.* at 15, 743 N.W.2d at 908 n.2.