STATE OF MICHIGAN
IN THE SUPREME COURT
Appeal from the Michigan Court of Appeals
Tukel, P.J., and Sawyer and Riordan, JJ.

VECTREN INFRASTRUCTURE SERVICES CORP.,

Plaintiff-Appellee,

v

MICHIGAN DEPARTMENT OF TREASURY,

Defendant-Appellant.
_____/

Supreme Court No. 163742

Court of Appeals No. 345462

Court of Claims No. 17-000107-MT

REPLY BRIEF OF APPELLANT MICHIGAN DEPARTMENT OF TREASURY

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INTRODUCTION

In its supplemental response brief, Vectren continues to presume, without proof, that there is unconstitutional distortion caused by application of the Michigan Business Tax (MBT) apportionment formula. Vectren claims that it has proof, but the documents it relies upon do not show what amount of Minnesota Limited, Inc.'s (MLI's) value is attributable to Michigan. Further, Vectren continues to rely on attorney-prepared documentation and also attaches new documentation that was not part of the lower court record, which, therefore, this Court should not consider. Finally, Vectren continues to ignore the statutory mandate that Treasury alone approve any alternative apportionment formula, thus effectively—and erroneously—claiming that the role a taxpayer may play in deciding this question warrants a court ordered negotiation between taxpayers and Treasury.

Vectren's arguments are without factual or legal support. Accordingly, this Court should reverse the Court of Appeals' decisions and affirm the Court of Claims' determination that Vectren is not entitled to alternative apportionment.

LAW & ARGUMENT

I. Vectren's purported evidence does not show gross distortion, and Vectren also impermissibly expands the record by attaching papers that were not part of the lower court record.

A. Vectren's purported evidence does not show distortion.

Vectren claims that the sales apportionment formula for tax year 2011 resulted in gross distortion to MLI. But Vectren fails to provide sufficient evidence

to support such an allegation. Throughout this entire litigation, Vectren has not once identified, with supporting documentation, what portion of the gain from the sale of MLI is attributable to Michigan. It has not provided any valuation study or expert witness opinion. Neither has it provided an independent metric for the value or gain on the sale of MLI that is attributable to Michigan. Instead, it relies on its past history and documentation that does not support its contentions.

The documents Vectren identifies do not show what value is attributable to Michigan, and, therefore, cannot show gross distortion. Vectren relies on the following documents:

Document	Description
Holcomb report	This is a summary document—not source evidence—generated by individuals with no foundation as to the question of, and does not show, the value or gain from the sale of MLI that is attributable to Michigan. Instead, this memorandum was prepared to promote the sale of MLI's business. The memorandum also discusses the benefit MLI stood to gain from renewed domestic attention to difficulty in accessing oil and gas deposits, and shale recovery techniques that included the Antrim Shale formation (located in Michigan), which is in MLI's "geographical sweet spot." (Appx Vol I, pp 127a–133a.[1]) In addition, according to the report, MLI had a facility in Illinois that served as a "beachhead for securing work in Michigan, Illinois, Indiana, and Missouri." (*Id*. at 169a.) This document, while it does infer the potential value and benefit that Michigan assets and location may have to a buyer of MLI, does not show what value or gain from the sale of MLI is attributable to Michigan.
KPMG valuation report	This is also a summary document—not source evidence—generated by individuals with no foundation as to the question of, and does not show, the value of MLI

[1] All appendix citations (Appx) are from the appendices that were attached to Treasury's May 4, 2022 brief on appeal.

	attributable to Michigan. The purpose of this report was to value MLI's intangible assets in order to comply with certain financial reporting requirements and tax regulatory purposes. (Appx Vol II, p 830a.) KPMG valued MLI's intangible assets based on future earnings generated by the use of the assets. (*Id*. at 823a–824a.) KPMG did not value any other assets. KPMG also did not value any intangible assets on a state-by-state basis. (*Id*. at 825a.) This document does not show what value or gain from the sale of MLI is attributable to Michigan.
Vectren Purchase Agreement	This is an agreement for Vectren Infrastructure Services Corporation's purchase of MLI and Nordic Land. This agreement identifies at a high level, and in general terms, revenue by customers, including Enbridge and Consumers Energy; preliminary net working capital; goodwill; MLI equipment; Nordic equipment; intellectual property; and contracts. This document does not show what value or gain from the sale of MLI is attributable to Michigan.
Enbridge contract	This establishes the business activity MLI carried out in Michigan, and, if anything, supports Treasury's position that MLI had the business activity as reported in Vectren's Michigan tax returns, for which reason there is no distortion.
U.S. tax returns	These federal tax returns identify at a high level, and in general terms, general categories and total amounts of income, expenses, capital gains, and adjusted basis of property sold. These returns do not show what value or gain from the sale of MLI is attributable to Michigan.
MLI financial statements	This is an independent auditor's report that identifies at a high level, and in general terms, assets, liabilities, retained earnings, income, and expenses of MLI for the years 2009 and 2010. This report does not show what value or gain from the sale of MLI is attributable to Michigan.
Personal Property Tax Reports	This document contains amounts reported for machinery and equipment, including "grand totals"—located in the Charter Township of Independence on the specific assessment dates of December 31, 2009 and December 31, 2010 (Tax Day days for the 2010 and 2011 tax years, respectively). No testimony or documentation has been provided that establishes that these are the only fixed assets located in the entire state of Michigan for the entire years of 2009 and 2010. Machinery and equipment can be moved in and out of the state of Michigan all year long and in multiple jurisdictions. Further, these documents do not

	show what value or gain from the sale of MLI is attributable to the state of Michigan.
Customer contract lists/valuations	This document is a portion of the Vectren Purchase Agreement previously discussed above. This document identifies contracts that either still had amounts payable to MLI in excess of $100,000 at the time of the preparation of this document, or contracts that resulted in payments in excess of $100,000 that still had a written warranty period. Contrary to Vectren's assertion, this document does not identify valuation amounts for intangibles or show what value or gain from the sale of MLI is attributable to the state of Michigan.
Lurie audited financial statements	This is the same document previously identified above as MLI's Financial Statements. Again, this report does not show what value or gain from the sale of MLI is attributable to Michigan.
Alternative minimum tax statements	This document appears to be a depreciation schedule purportedly identifying assets and placed in service dates. However, this document does not clearly identify what these assets are or where they were used. Further, this document does not show what value or gain from the sale of MLI is attributable to the state of Michigan.
Deposition transcripts of Bradley Hirsch, Douglas Banning, Christopher Leines, Jeffrey Starbird	This is self-serving testimony, not source documentation, that does not establish the value of the business or Michigan's contribution.

In short, this "documentation", which Vectren describes as "only a portion of the over 1,200 pages of business records submitted," does not "support[ ] the clear and cogent evidentiary standard." (Vectren's Br, p 14.) Neither does Vectren's citation to MRE 803(6)—a rule for hearsay exceptions—or the mere fact of a Treasury audit (*id.*), (which relied on Vectren's own reported business activity, per its Michigan tax return), support Vectren's assertion.

B. Vectren impermissibly seeks to expand the appellate record.

Vectren attaches various documents to its supplemental brief that were not part of the lower court record—i.e., never filed with the Court of Claims and never entered as exhibits to Vectren's pleadings or its response to Treasury's motion for summary disposition. Further, these documents were not attached to Vectren's appellate briefs in the Court of Appeals.

MCR 7.310(A) provides that "[a]n appeal is heard on the original papers, which constitute the record on appeal." Further, "[w]hen requested by the Supreme Court clerk to do so, the Court of Appeals clerk or the lower court clerk shall send to the Supreme Court clerk all papers or electronic documents on file in the Court of Appeals or the lower court, certified by the clerk." MCR 7.310(A)(1).

Here, Vectren has attached various exhibits to its appellate brief that were not filed with the Court of Claims, not part of any deposition transcripts, and not attached as exhibits to Vectren's pleadings or its response to Treasury's motion for summary disposition. Specifically, Vectren attaches for the first time:

- **MLI state tax returns, other than Michigan**[2]: These documents were not attached to any pleadings or briefs in the Court of Claims (or the Court of Appeals). Even if this Court considers these documents, this still does not identify what assets were located in Michigan. The various state taxing jurisdictions employ different forms of apportionment and allocation to their states. Some states' tax forms use a three-factor apportionment formula that identifies a value of assets located in that state, but other states employ different tax taxing schemes. Accordingly, these documents do not establish

[2] Vectren's Michigan tax returns are part of the Court of Claims record because they were attached to Treasury's motion for summary disposition briefing.

what assets were used in Michigan. In addition, these tax returns do not include supporting schedules or documentation.

- **MLI Depreciation schedules and fixed asset reports**: These documents have the same bates numbering as documents that were part of the Court of Claims record (VEC 000408–000438), but they are not the same documents. Even if considered, these documents are schedules that do not show where the tangible assets were located, only that MLI unloaded certain tangible assets at the end of their useful life and depreciation value, and they contained *no supporting schedules or documentation*.

- **MLI Disposal schedules**: These documents have the same bates numbering as documents that were part of the Court of Claims record (VEC 000719–000744), but they are *not the same documents* and were not part of the lower court record. Even if considered, these documents are schedules that do not show where the tangible assets were located, only that MLI unloaded certain tangible assets at the end of their useful life and depreciation value, and they contain *no supporting schedules or documentation*.

Accordingly, Treasury asks this Court not to consider these documents.

II. Vectren has not shown unconstitutional taxation, relying instead on an historical analysis and ignoring that MLI's value contemplates future opportunities/growth, including in Michigan.

In arguing that the statutory apportionment formula results in unconstitutional taxation, Vectren again points to the past, ignoring that taxation relates to the particular tax year and that the value of the business's intangible assets and goodwill are determined at the time of the sale and look to future

opportunities. Neither is the constitutionality of taxation measured by a comparison between the current tax year and past years.[3]

Vectren admits that it "carried on business in Michigan and therefore, is subject to taxation." (Vectren's Br, p 16.) But then, Vectren again rehashes its tax percentage from 2001 through 2010 and computes an average tax percentage. "The statutory formula results in an apportionment formula that exceeds a tenfold increase of the average." (*Id*. at 17.) Vectren then compares this case to *Hans Rees' Sons, Inc v North Carolina*, 283 US 123 (1931). But *Hans Rees* did not compare the taxpayer's tax amounts for the years in issue with prior years' tax amounts. Instead, after the Court examined an analysis submitted by the taxpayer showing the taxpayer's business activities and income during the years in issue (1923–1926), the Court determined that "where a corporation manufactures in one State and sells in another," apportionment of income to one state (North Carolina), which represented only 21.7% of the taxpayer's income, was out of proportion to the business transacted in that state. 283 US at 132, 135–136.

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[3] Vectren again relies on its attorney-prepared letter to support its argument that the statutory formula results in distortion. (Vectren's Br, p 17 n 4.) Vectren asserts that "Treasury's argument dismisses the magnitude of an attorney's signature on a document," and cites MCR 2.114(D). (*Id*.) This Court Rule was repealed as of 9/1/2018 and replaced by MCR 1.109(E)(5), and neither the old nor the new Court Rule provides that an attorney's representations are evidence, because they are not. *People v Benton*, 294 Mich App 191 (2011). Vectren draws a meaningless distinction in asserting that *Benton* involved a confrontation clause issue and did not deal with the weight given to an attorney-prepared document. (*Id*.) But this ignores that, regardless of context, ipse dixit attorney statements are not evidence. See also *People v Graves*, 458 Mich 476 (1998) and *People v Dobek*, 274 Mich App 58, 66 n 3 (2007) (affirming jury instructions that attorney statements are not evidence.).

This examination of *only the years in issue* makes sense: the question is not whether taxation in the current year is distortive *in relation to taxation of prior years*. Treasury does not tax the past, and past years' taxation percentages are not a reliable metric for the value of a business and its activities *in the current year*. Instead, the question is whether the formula is distortive in relation to the current year's business realities. *Id*. In analyzing the past, Vectren ignores the central question, and, therefore, cannot satisfy its burden.

But even taking Vectren's legal theory at face value, Vectren does not point to any source evidence showing that the value of the business related to Michigan is distortive. Instead, it identifies two summary statements and self-serving deposition testimony. (Vectren's Br, pp 19–20.) And while Vectren points to the Enbridge contract, the ipse dixit characterization that "the contract was anomalous" (*id*. at 20) does not change the amount of business done in Michigan in the tax year at issue or the footprint that Michigan had in MLI's business valuation.

Finally, Vectren's argument that inclusion of the gain at issue in the tax base but not the sales factor creates distortion (*id*. at 22–23) is not supported by any statutory or case law. Instead, Vectren relies on "Michigan tax practitioners," who "have discussed such asymmetry" divorced from the statutory formula or any case law support. (*Id*. at 22.) This is yet another attempt to present the work of stakeholding attorneys as if it were evidence or legal support for Vectren's argument. In short, to include the sale in the apportionment formula, Vectren must first determine what portion is attributable to Michigan. It fails to do so.

III. The MBT gives Treasury the exclusive authority to approve any alternative apportionment, and the Court of Appeals' decisions contradict the statute and create separation-of-powers problems.

Vectren compounds the error of the Court of Appeals' decisions, ignores the separation of powers problems these decisions create, and mischaracterizes Treasury's argument and alternative apportionment process. First, Vectren claims that "the remand anticipates that only if the parties be unable to reach consensus, would judicial intervention to be appropriate." (Vectren's Br, p 23.) But this presupposes that the parties must reach a consensus, ignoring that the statute MCL 208.1309(2), gives Treasury the exclusive authority to approve any alternative apportionment method. The courts cannot force Treasury into negotiation with taxpayers, as that would constitute legislative activity carried out by the judiciary—a separation-of-powers problem that Vectren ignores.

Further, Vectren posits a strawman argument in place of Treasury's actual argument. According to Vectren, "Treasury argues that MCL 208.1309(2) requires taxpayers be removed from the process." (Vectren's Br, p 23.) But Treasury has never argued that taxpayers be removed from the process. As Treasury's Revenue Administrative Bulletin (RAB) 2018–28 (cited by Vectren), contemplates, taxpayers may have a role in the process, but that role is limited to making proposals regarding alternative apportionment methods, which do not bind Treasury. It is Treasury that has the exclusive statutory authority to approve and/or reject any proposal, or determine its own method, and otherwise cannot be forced into negotiation. And while "there is no reason, statutory or otherwise, that would prohibit the department and the taxpayer to collaborate to determine a reasonable

alternative apportionment method," (*id*. at 24), this cannot be forced upon Treasury given its exclusive approval authority. Problematically, the Court of Appeals' decisions not only contemplate but explicitly order Treasury to negotiate with Vectren, and for the parties' resolution (instead of Treasury's decision, which the statute contemplates) to be subject to judicial review.

CONCLUSION & RELIEF REQUESTED

The Court of Appeals' decisions are erroneous as a matter of law, rely on purported facts that are not in evidence and create separation-of-powers problems.

Accordingly, Treasury respectfully asks that this Court reverse the Court of Appeals' decisions and affirm the Court of Claims' determination that Vectren is not entitled to alternative apportionment.

Respectfully submitted,

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