STATE OF MICHIGAN
IN THE SUPREME COURT
Appeal from the Michigan Court of Appeals
Fitzgerald, P.J., Wilder and Murray, JJ.

ANDRIE INC.,

Plaintiff-Appellee,

v

DEPARTMENT OF TREASURY,

Defendant-Appellant.

Supreme Court No. 145557

Court of Appeals No. 301615

Court of Claims No. 08-95-MT

The appeal involves a ruling that a provision of the Constitution, a statute, rule or regulation, or other State governmental action is invalid.

REPLY BRIEF OF APPELLANT DEPARTMENT OF TREASURY

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INTRODUCTION

It is undisputed that Andrie used, stored, or consumed tangible personal property in Michigan. Under the Use Tax Act's plain language, Andrie is thus liable for use tax *unless* it proves it is entitled to a use-tax exemption, which requires proof that sales tax was paid for the tangible personal property when purchased. MCL 205.94(1)(a). Andrie is confused about this issue in three ways.

First, Andrie misidentifies the taxable event at issue. Andrie argues that the taxable event is the retail transaction. But the taxable event or transaction is Andrie's use, storage, or consumption of tangible personal property in Michigan.

Second, Andrie argues that there is never use tax liability on the use, storage or consumption of tangible personal property if the property is purchased in a Michigan retail transaction. But that is not at all what the Use Tax Act actually says.

Third, Andrie says that a retail purchaser is entitled to a presumption that sales tax is paid. But there is no such law, other than the Court of Appeals' statement below. This Court should reverse.

ARGUMENT

I. There is no use-tax exemption based on the fact that the tangible personal property consumed was purchased in a retail transaction "subject to" sales tax.

In the very first sentence of its brief, Andrie states that "the parties agree that Michigan sales tax applies to all the transactions at issue." This is not true. Treasury agrees that the Sales Tax Act imposes a 6% tax on the *retail* sale of tangible personal property in Michigan. Treasury also agrees that the 6% use tax is not assessed on a *retail* transaction. But this case does not involve an assessment of sales tax on the retail sale of tangible personal property in Michigan. It involves Andrie's use, storage, or consumption of tangible personal property in Michigan. The activity that triggers Andrie's tax liability is not the retail sale, but Andrie's use of the property. The issue is whether Andrie qualifies for a use-tax *exemption.*

Andrie's misunderstanding is rooted in a prior version of the Use Tax Act, one that is no longer part of Michigan law. As it appeared in the Compiled Laws of 1948, the predecessor to MCL 205.94(1)(a) *did* contain an exemption for tangible personal property "subject to" sales tax:

> The tax hereby levied shall not apply to: (a) Property the sale of which in this state has been *subjected to* the tax imposed by Act No. 167 of the Public Acts of 1933, as amended. [Emphasis added.]

But in 1949, the Legislature removed the "subjected to" language and replaced it with a different exemption, one that requires proof that sales tax had been "paid":

> Property sold in this state on which transaction a tax *has been paid* under the provisions of Act No. 167 of the Public Acts of 1933, as amended. [Emphasis added.]

Subsequent revisions in 1953, 1970, 1978, and 2002 consistently maintained the proof-of-payment requirement, resulting in the language that controls this case:

> Property sold in this state on which transaction a tax *is paid* under the general sales tax act, 1933 PA 167, MCL 205.51 to 205.78, if the tax was due *and paid* on the retail sale to a consumer. [MCL 205.94(1)(a) (emphasis added).]

Andrie has latched onto the "subject to" language in the 1948 statute. But no provisions in the current Use Tax Act support Andrie's position. Andrie's position is likewise not supported by the case law Andrie cites.

In *World Book v Dep't of Treasury*, 459 Mich 403, 590 NW2d 293 (1999), the taxpayer was an out-of-state company that sold encyclopedias to Michigan residents via door-to-door sales. The salespersons took orders and deposits from Michigan residents for encyclopedias in Michigan. The orders were then sent to the plaintiff's headquarters in Illinois for approval and the encyclopedias were shipped from the inventory in Illinois to the customer in Michigan. The case involved two issues that are factually and legally distinct from this case. The first issue was whether there was a retail sale in Michigan. The second issue was, if the retail sale took place in Illinois, whether the use tax applied. So the exemption to the Use Tax Act that the court considered in *World Book* was the exemption for the *payment of sales tax to another State*. MCL 205.94(1)(e). There are no similar issues in the present case, as both parties agree that Andrie acquired the personal property at issue in a retail sale in Michigan. Despite this, Andrie cites to language in the opinion regarding the Court's analysis of whether the retail sale occurred in Michigan or Illinois as supportive of its position. In doing so, Andrie mischaracterizes this Court's position as it related to the applicability of use tax. This Court affirmed that use tax does

not apply to property sold in Michigan "on which Michigan sales tax has already been *paid*." 459 Mich 403, 408-409 (1999) (emphasis added). *World Book* supports Treasury's position, not Andrie's.

Lockwood v Commissioner of Revenue, 357 Mich 517; 98 NW2d 753 (1959), involved a challenge to the constitutionality of PA 1959, No. 263. At issue was whether the Legislature had violated the Michigan Constitution when it had adopted an additional 1% use tax that operated as a sales tax and, therefore, exceeded the constitutional 3% sales tax limit in place at the time. That issue has nothing to do with the dispute here. What is pertinent is that *Lockwood* involved an in-State retail sale, evidencing that all parties acknowledged that the use tax applies to in-State sales. Nowhere in the opinion does this Court say that the imposition of the use tax is improper or is otherwise inapplicable if the property at issue is acquired in an in-State retail transaction. Like *World Book, Lockwood* supports Treasury's position, not Andrie's.

II. There is no presumption that sales tax was paid as part of the sales price in a Michigan retail sale.

Andrie also tells this Court that it is "well settled" and "well-established" Michigan law that a purchaser is entitled to a presumption that it paid the sales tax on an in-State retail transaction. Not so.

Andrie's position in this case and reliance on MCL 205.73 and *Swain Lumber v Newman Development*, 314 Mich 437; 22 NW2d 891 (1946)[1] was rejected by the

[1] Treasury was not a party to *Swain Lumber*.

Michigan Tax Tribunal in *Kruszka v Dep't of Treasury*, MTT Docket No. 88327 (November 13, 1986). In *Kruszka*, the taxpayers purchased a sailboat in Michigan from a Michigan retailer upon which no sales tax had been paid or remitted to the State. The taxpayers' primary claim was that the seller's obligation to collect and remit sales tax on the transaction absolved them of their liability for use tax. Like Andrie, the taxpayers relied on MCL 205.73 and *Swain Lumber*. The Tax Tribunal held that "while MCL 205.73; MSA 7.544 and *Swain Lumber* do purport to address the question of sales tax liability on the part of a seller in a given situation, neither offers guidance relative to the precise question presented herein, i.e., whether the instant purchasers are liable for use tax." *Id.* at p. *16. The Tax Tribunal instead relied on *Terco v Dep't of Treasury*, 127 Mich App 220; 339 NW2d 17 (1983), which correctly held that a purchaser may incur use tax liability where a sales tax has not been "paid" on an in-State transaction. *Id.* at *15-18.

Andrie's reliance on *Sims v Firestone Tire & Rubber Company*, 397 Mich 469; 245 NW2d 13 (1976), is likewise misplaced.[2] *Sims* involved a class action brought by purchasers of services who claimed to have been unlawfully charged sales tax when the retailer sought to recoup a tax penalty assessed against him for failing to maintain adequate books and records. This Court focused on whether a penalty could be treated as a tax for purposes of MCL 205.73, which allows the retailer to reimburse himself for taxes. The facts and issues are totally inapposite to the case at bar. Yet Andrie cites to the portion of *Sims* where this Court discusses the nature of the penalty and whether the Legislature intended to include the penalty

[2] Treasury was not a party by the time *Sims* reached this Court.

when it used the word "taxes" in MCL 205.73. This Court did not address, nor did it rule on, whether the consequence of a retailer being able to reimburse itself for taxes and penalties under MCL 205.73 means that the Sales Tax Act contains a presumption that a sales price includes sales tax. *Sims* does not involve the use tax, and the word presumption appears nowhere in the opinion.

Equally inapposite is *Laurentide Leasing Co v Schomisch*, 382 Mich 155; 169 NW2d 322 (1969).[3] *Laurentide* is basically an escrow/agency case. It involves a dispute concerning sales-tax liability arising out of the sale of laundry equipment. The bank acted as an escrow agent for both the seller and the purchaser. The bank failed to communicate an amended offer made by the seller that the sales price was $43,000, plus Michigan sales tax. The purchasers paid the bank, as escrow agent, $43,000, and they received a bill of sale conveying good title to the equipment. Subsequently, the seller was required to pay sales tax on the transaction and filed a lawsuit against the bank to recoup the sales tax. This Court found that the seller could recover from the bank because the bank had breached its duty to the seller by releasing the bill of sale to the purchaser without having first received the sales tax on the transaction. *Laurentide* does not stand for the proposition that there is a presumption in Michigan law that sales tax is included in the sales price of goods.[4]

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[3] Treasury was not a party to *Laurentide*, either.

[4] The same is true for Andrie's reliance on RAB 1990-24, in which Treasury provides guidelines to veterinarians who render services (nontaxable) and make retail sales (taxable). Similarly, OAG 5998 simply provides that the legal incidence of sales tax fall on the retailer. Treasury does not contend that Andrie is liable for sales tax. Andrie also cites for support a Letter Ruling which has been withdrawn from publication. RAB 2000-6 explains that "[t]he Department will periodically withdraw Letter Rulings from publication that are not good examples. A Letter

There is a distinction between a presumption at law that sales tax is included in the price of goods sold and the recognition that a retailer may include the amount of tax in the selling price. There is no evidence in this case that the retailers who sold the personal property to Andrie included sales tax in the selling price. If Andrie could demonstrate it paid sales tax, Treasury agrees Andrie would be exempt from use tax under MCL 205.94(1)(a). But Andrie has the burden of proving its entitlement to an exemption, and it has failed to meet that burden.

III. MCL 205.94(1)(a)'s use-tax exemption does not apply here.

Andrie does not attempt to argue that it is exempt from use tax (Andrie Br., p 12), nor could it, because Andrie has failed to offer proof that sales tax was "paid" on the tangible personal property that Andrie used and consumed as the statute requires. Instead, Andrie incorrectly states that MCL 205.94(1)(a) is not an exemption. Andrie is forced to take the position to avoid this Court's well-settled case law that taxpayers bear the burden of proving entitlement to an exemption. *Michigan Baptist Home & Development Co v Ann Arbor,* 396 Mich 660, 670; 242 NW2d 749 (1976); *Elias Bros Restaurants, Inc v Treasury Dep't,* 452 Mich 144, 150, 549 NW2d 837 (1996). ("Because tax exemptions are disfavored, the burden of proving entitlement to an exemption rests on ... the party asserting the right to the exemption.")

Ruling ceases to be a good example when changes in the law cause the Letter Ruling to become obsolete, or when the Department determines that the Letter Ruling confuses rather than assists the public."

But MCL 205.94, entitled "*Exemptions* from tax; particular property or services," does set forth many of the statutory exemptions from use tax. MCL 205.94 (1)(a)-(1)(y). The statute's plain language contradicts Andrie's position that MCL 205.94(1)(a) is not an exemption to use tax. Having failed to satisfy its burden of proving its entitlement to the statutory exemption, Andrie is liable for use tax here.

IV. Imposition of use-tax in these circumstances does not constitute double taxation.

One of Andrie's primary themes is that Treasury is attempting to double tax the same transaction. That is incorrect. As explained above and in Treasury's initial brief, the sales tax and use tax apply to different transactions (sale and use). And, by virtue of the MCL 205.94(1)(a) exemption, the two taxes are entirely complementary. Treasury does not care if it receives the 6% tax from the retailer or from the user. But Michigan law ensures that Treasury receives it from someone. And under the statutory scheme, it is not Treasury's burden to demonstrate whether Andrie paid sales tax; it is Andrie's burden to prove sales tax has been "paid." MCL 205.94(1)(a) does not require a consumer to prove that the retailer remitted the sales tax to the State, although such proof would also suffice; it is enough for the consumer to prove that it paid sales tax to the retailer.

Importantly, this Court's affirmance of Andrie's use-tax liability does not place Andrie in a Catch-22 where it must gain access to a vendor's records and prove that the vendor paid sales tax to the State. To prove the exemption, Andrie need only present a receipt that proves that sales tax was "paid." That payment

could be Andrie's payment of the sales tax to the vendor, or it could be a statement that the vendor is remitting sales tax to the State. Either way, the burden is nominal and avoids the problem the Legislature tried to avoid when it enacted these tax provisions-forcing Treasury to audit a taxpayer's countless vendors to determine the taxpayer's use-tax liability. It is Andrie that seeks the unworkable result, not Treasury.

CONCLUSION AND RELIEF REQUESTED

There are two separate taxable events that give rise to the sales tax and the use tax. The purchase of tangible personal property gives rise to sales-tax liability, and consumption and use of that property gives rise to use-tax liability. Nevertheless, the Legislature exempts a party from use-tax liability if it can show that sales tax was actually "paid" on the tangible-personal-property sale. That burden is undemanding; it simply requires a party subject to use-tax liability to produce a receipt which shows the payment of sales tax on the tangible personal property used or consumed. But Andrie has failed to satisfy that easy burden.

Affirming the Court of Appeals will have tremendous adverse consequences on the State and the public fisc. First, affirmance would require Treasury to reveal confidential tax records of other taxpayers (retailers) to a taxpayer seeking to avoid use-tax liability. Second, affirmance would shift the long-standing burden of proof imposed on taxpayers seeking an exemption. Third, affirmance would force Treasury to audit dozens or even hundreds of vendors simply to determine whether any individual taxpayer has satisfied its use-tax obligation. Thankfully, all of these

consequences can be avoided simply by applying (1) the Use Tax Act's plain language, and (2) the burden of proof that this Court has always imposed on taxpayers claiming entitlement to an exemption.

Accordingly, Treasury respectfully requests that the Court vacate Paragraph II.C of the Court of Appeals' April 26, 2012 opinion and hold that Andrie is liable for use tax unless it can prove that sales tax has been paid on the tangible personal property Andrie used and consumed.

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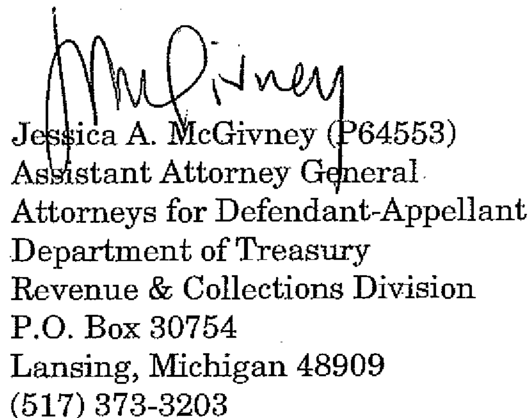

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