STATE OF MICHIGAN
DEPARTMENT OF LICENSING & REGULATORY AFFAIRS
MICHIGAN ADMINISTRATIVE HEARING SYSTEM
MICHIGAN TAX TRIBUNAL

Great Lakes International Recycling,
Petitioner,

v

MTT Docket No. 410961

Michigan Department of Treasury,
Respondent.

Tribunal Judge Presiding
Steven H. Lasher

FINAL OPINION AND JUDGMENT

INTRODUCTION

Petitioner, Great Lakes International Recycling, appeals a final assessment under the Use Tax Act levied by Respondent, the Michigan Department of Treasury, based on an audit for the January 1, 2000 through August 31, 2009 tax periods. A hearing on this matter was held on May 8, 2012. Scott Mudford, CPA, represented Petitioner, and Jack M. Panitch, Attorney, represented Respondent. The sole witness was Michael Mione, Petitioner's controller.

Following the hearing, the parties were requested to submit briefs on whether or not reasonable cause existed for a penalty waiver under MCL 205.23(3), and whether or not *Andrie v Dep't of Treasury*, 296 Mich App 355; 819 NW2d 920 (2012) applied. This case was then placed in abeyance on June 26, 2012, pending final resolution of *Andrie*. The Michigan Supreme Court issued its decision in *Andrie* on June 23, 2014.

The hearing in this case was conducted by Tribunal Member B.D. Copping. Judge Copping is no longer a Tribunal Member at the Tax Tribunal; as a result, this Opinion is being rendered by Tribunal Chair Steven H. Lasher.

Based on the evidence, testimony, and case file, and as discussed in detail below, the Tribunal finds the assessment to be as follows:

Assessment No.	Tax	Penalty	Interest
S257356	$141,495[1]	$14,150	*

*Interest to be computed in accordance with 1941 PA 122.

[1] Tax, penalty, and interested to be further reduced based on Petitioner's payment of $99,002 on October 8, 2010, and any other payments Petitioner may have made with respect to this assessment.

PETITIONER'S CONTENTIONS

Petitioner contends that the parties are in agreement as far as what was industrial processing and what was not. Petitioner further contends that reasonable cause existed for waiver of the 10% negligence penalty and that the 2003 and 2004 tax years are beyond the statute of limitations as Petitioner filed Sales, Use, and Withholding returns for both years. In its Brief, Petitioner argued that Respondent is required under the Revenue Act to issue administrative rules and guidance establishing the threshold for the imposition of penalties and the mandatory waiver of the negligence penalty when a taxpayer establishes reasonable cause. Petitioner contends that the negligence standard set forth in RAB 2005-3 for imposition of the penalty "is that the taxpayer did not exercise due care by reading the instructions for filing tax returns before making a determination of their tax liability." Petitioner asserts that the RAB and examples "are heavily reliant on the taxpayer's duty to read the instructions promulgated by Respondent," but the instructions for the annual use tax return "say relatively nothing . . . [and] reading [the instructions] would be of virtually no aid to anyone in properly determining even the simplest business' Use Tax liability." Petitioner also argues in its Brief that the instructions for use tax are contrary to Respondent's stated position, *i.e.* that the negligence penalty was applied because Petitioner does not have a valid use tax license. Petitioner asserts that the testimony of its controller, Michael Mione, established that there were policies in place to limit the applicability of use tax and that he had a "better than average understanding" of the use tax but was unable to determine the answer to "very technical issues, which were the cause of the vast majority of the audit exceptions."

With respect to the limitations period, Petitioner argues that the record before the Tribunal reflects that returns were filed for all of the years in question. Petitioner further argues that Respondent's position regarding the lack of a valid use tax license is discredited by the instructions to the returns.

Lastly, regarding the applicability of the Court of Appeals decision in *Andrie*, Petitioner concedes that items purchased under an exemption certificate from the collection of sales tax would make those purchases subject to use tax. However, Petitioner contends that Respondent's audit "includes trucks and trailers which were licensed and operated on the public roads [and Respondent] indicated that if Petitioner could not show proof that the tax was paid, that

Petitioner was liable for the use tax on the purchase." Petitioner argues that "it is clear" from review of its records and its prepared Fixed Asset Exceptions report, that there are several Michigan vendors from whom Petitioner purchased over-the-road equipment. Petitioner included in its Brief a list of eight vendors with retail sales to Petitioner in Michigan that Petitioner believes should be exempt from use tax under *Andrie*.

PETITIONER'S ADMITTED EXHIBITS

No exhibits offered or admitted.

PETITIONER'S WITNESS

Petitioner presented the testimony of Michael Mione, CPA and Petitioner's controller. Mr. Mione testified that: (i) he has been the controller for Great Lakes International Recycling since 1999, (ii) it was his understanding that the company qualified for the industrial processing exemption "because of the nature of the business" [Transcript at 9], (iii) the internal policy relative to the trucks and trailers that make up a large part of the audit "wasn't real clearly defined" since all the vehicles had plates on them, which means they all had sales tax paid in order to be able to drive them on the road [Transcript at 10], (iv) he did inform the auditor that tax had been paid to the Secretary of State, but he did not have the files for all of the purchases going back ten years, (v) his prior experience is in the garbage industry and he talked with people in the recycling industry regarding what was taxable and what was not, (vi) he did not check to determine if Petitioner was registered for payment of use tax because he thought everything was in place, (vii) he did not check to see if use tax returns were being filed or if use tax was being reported until he was informed by the CPA firm in 2005 or 2006. [Transcript at 8 – 24.]

RESPONDENT'S CONTENTIONS

Respondent contends that Petitioner was not registered for payment of use tax, the use tax portion of the returns was not filled out, and there was no attempt by Petitioner to ascertain its use tax liability. In its Brief, Respondent argues that Petitioner must show that it acted with ordinary business care and prudence to establish reasonable cause for waiver of the negligence penalty. Respondent asserts that Petitioner's controller testified that he had not read the Michigan statutes prior to the audit and that his due diligence was done through talking with people in the industry; Respondent argues that this does not meet the definition of reasonable

cause and that there was a duty to "investigate and understand the language and scope of the tax laws." Further, Respondent asserts that "[o]rdinary business care and prudence dictated that the company at least inform itself about what the State had to say about the issue."

With respect to the 2003 and 2004 tax years, Respondent states that Petitioner was not registered for sales and use tax and made no effort to fill out the sales or use tax lines of the returns "and, therefore, did not file a return that would initiate the period of limitations on assessment." Respondent cites to *Estate of Lohman v Commissioner,* T.C. Memo 1972-27 with regard to what constitutes a return.

Lastly, Respondent's position is that *Andrie* is not similar to the present case and would not apply since Petitioner made purchases under an industrial processing exemption, representing to the vendors that its purchases were exempt from tax.

RESPONDENT'S ADMITTED EXHIBITS

R-1 2003 Annual Return for Sales, Use and Withholding Taxes (undated, page 1 only)
R-2 2004 Annual Return for Sales, Use and Withholding Taxes (undated)
R-3 2005 Annual Return for Sales, Use and Withholding Taxes
R-4 2006 Annual Return for Sales, Use and Withholding Taxes
R-5 2007 Annual Return for Sales, Use and Withholding Taxes, dated February 28, 2008
R-6 2007 Annual Return for Sales, Use and Withholding Taxes, dated February 2, 2008
R-7 2008 Annual Return for Sales, Use and Withholding Taxes, dated February 4, 2009
R-8 2008 Annual Return for Sales, Use and Withholding Taxes (undated, page 1 only)
R-9 2009 Annual Return for Sales, Use and Withholding Taxes, dated February 3, 2010
R-10 2009 Annual Return for Sales, Use and Withholding Taxes, dated February 26, 2010

FINDINGS OF FACT

1. Petitioner operates a single-stream recycling business.
2. Petitioner purchased trucks, trailers, and roll-off containers for use in its business.
3. Petitioner did not pay tax on the purchase of the roll-off containers, believing that the industrial processing exemption applied.
4. Petitioner is appealing the assessment of use tax, penalties, and interest, assessed by Respondent for the January 1, 2000 to August 31, 2009 tax periods.
5. An Intent to Assess was issued on September 8, 2010 as follows:

Assessment No.	Tax	Penalty	Interest
S257356	$168,184	$17,857[2]	$62,044.15

6. Petitioner made a payment of $92,002 on October 8, 2010. According to Respondent, this payment was applied as $11,670.02 to tax, $17,857 to penalty, and $62,474.98 to interest.[3]

7. The Final Assessment, issued on November 17, 2010 is as follows:

Assessment No.	Tax	Penalty	Interest
S257356	$156,513.98	$0	$564.95

8. Petitioner was not registered for the payment of sales or use tax.

9. Petitioner's 2003 and 2004 Sales, Use, and Withholding tax returns do not reflect any amounts in the columns for sales tax or use tax and only contain amounts for withholding tax.

10. As contained in Respondent's Brief, the parties have agreed that then audit should be revised and the total assessment for each tax period should be as follows (absent any reductions relative to Petitioner's specific arguments before the Tribunal):

CY 2000	$15,009
CY 2001	$12,097
CY 2002	$13,166
CY 2003	$15,264
CY 2004	$11,948
CY 2005	$16,585
CY 2006	$27,481
CY 2007	$25,225
CY 2008	$25,770
1/1/2009 – 8/31/2009	$6,162
TOTAL	$168,707

CONCLUSIONS OF LAW

The assessment at issue was imposed under the Use Tax Act ("UTA"), MCL 205.91 *et seq*. The use tax is a ". . . specific tax for the privilege of using, storing, or consuming tangible personal property in this state at a rate equal to 6% of the price of the property. . . ." MCL 205.93(1). MCL 205.97(1) provides that "[e]ach person storing, using, or consuming in this state tangible personal property or services is liable for the tax levied under this act and that

[2] Respondent's Brief reflects that at some unspecified point prior to the Intent to Assess, the original amount of use tax assessed against Petitioner was $178,564. [Respondent's Brief at #15]

[3] Respondent's Prehearing Statement, filed December 5, 2011.

liability shall not be extinguished until the tax levied under this act has been paid to the department."

The parties indicated at the hearing that they are in agreement with respect to what constitutes industrial processing and what does not in terms of revisions to the audit. As stated in Respondent's Post-Hearing Brief, the parties have agreed that the audit should be revised to reflect a total tax liability of $168,707, which necessarily would be reduced further should Petitioner prevail in any of its arguments presented to the Tribunal. Further, the revised tax amount of $168,707 does not reflect the $99,002 payment made by Petitioner on October 8, 2010.

Although the parties may have reached an agreement as to a reduction in the tax amount reflected in the audit, three specific issues remain that must be addressed by the Tribunal: (1) the statute of limitations on the 2003 and 2004 tax years; (2) the application of the 10% negligence penalty under MCL 205.23(3) and whether there exists reasonable cause for a penalty waiver; and (3) the applicability of *Andrie* following the determination of the Michigan Supreme Court.

Statute of Limitations on 2003 and 2004 tax years

MCL 205.27a(2) states, in relevant part:

> A deficiency, interest, or penalty shall not be assessed after the expiration of 4 years after the date set for the filing of the required return or after the date the return was filed, whichever is later. The taxpayer shall not claim a refund of any amount paid to the department after the expiration of 4 years after the date set for the filing of the original return.

Part of Respondent's argument for inclusion of the 2003 and 2004 tax years in the audit is that Petitioner was not registered for use tax, as required by MCL 205.95(1). In addition, Respondent contends that Petitioner failed to fill out the sales and use tax lines of the 2003 and 2004 Annual Sales, Use, and Withholding tax returns. According to Respondent, the failure to complete the lines for sales and use tax does not constitute a "return" that would be sufficient to start the running of the statute of limitations.

The Tribunal finds that 2012 PA 211 amended MCL 205.27a to include the following provision, "(12) [t]he filing of a return includes the filing of a combined, consolidated, or

composite return whether or not any tax was paid and whether or not the taxpayer reported any amount in the tax line including zero." [Emphasis added.] Section (12)[4] is retroactive and:

> Is effective for all tax years that are open under the statute of limitations provided in section 27a of 1941 PA 122, MCL 205.27a, for all matters regarding the filing of a return under this section. However, this amendatory act is not intended to affect a refund required by a final order of a court of competent jurisdiction for which all rights of appeal have been exhausted or have expired before May 1, 2012.

The 2003 and 2004 tax years are still "open" under MCL 205.27a(3), as an appeal of the final assessment is being heard by the Tribunal. Regardless of whether or not Petitioner was registered for use tax, Petitioner did file the combined Annual Sales, Use, and Wittholding tax returns for both 2003 and 2004, although there were no values in the sales or use tax columns. Under MCL 205.27a(13), Petitioner properly filed a return, even though it did not report any amount in the tax lines for use tax. The Tribunal finds that since the returns for 2003 and 2004 are considered to have been filed pursuant to MCL 205.27a(13), those tax years are not properly contained within the audit, as this would be beyond the 4-year statute of limitations. Based on the breakdown of the revised audit values agreed upon by the parties, the final assessment shall not include the amount of $15,264 relating to the 2003 tax year and $11,948 relating to the 2004 tax year.

Negligence penalty under MCL 205.23(3)

> MCL 205.23(3) provides, in relevant part:
>
> [I]f any part of the deficiency or an excessive claim for credit is due to negligence, but without intent to defraud, a penalty of $10.00 or 10% of the total amount of the deficiency in the tax, whichever is greater, plus interest as provided in subsection (2), shall be added . . . . If a taxpayer subject to a penalty under this subsection demonstrates to the satisfaction of the department that the deficiency or excess claim for credit was due to reasonable cause, the department shall waive the penalty. [Emphasis added.]

The Michigan Administrative Code, specifically ACR 205.1012(1), defines "negligence" in this context as follows:

> Negligence is the lack of due care in failing to do what a reasonable and ordinarily prudent person would have done under the particular circumstances. The standard for determining negligence is whether the taxpayer exercised ordinary care and prudence in preparing and filing a return and paying the

[4] MCL 205.27a has undergone further amendments, and this language is now contained in subsection (13).

> applicable tax in accordance with the statute. The facts and circumstances of each case will be considered.

Petitioner asserts that under RAB 2005-3, "the standard for the imposition of the tax is that the taxpayer did not exercise due care by reading the instructions for filing tax returns before making a determination of their tax liability." However, the negligence standard under the Revenue Act and Administrative Code encompasses more than merely the exercise of due care by reading the instructions for the return. The proper focus under the Revenue Act and Administrative Code is whether the taxpayer can demonstrate a reasonable excuse (*i.e.*, reasonable cause) for deviating from the standards normally expected of taxpayers (*i.e*, "what a reasonable and ordinarily prudent person would have done under the particular circumstances"). Petitioner's controller testified that he began his position in January of 1999. His testimony reflects that: (i) he did not review the Michigan statutes (until just recently); (ii) there were not any clearly defined policies in place for the trucks and trailers purchased; (iii) he never checked to see if the company was registered for payment of use tax, (iv) and he did not check to determine whether a use tax return was being filled out until the CPA firm advised him in 2005 or 2006. The Tribunal finds that the actions of Petitioner fall below what a reasonable and ordinarily prudent person would have done in these circumstances. A reasonable person in this situation would have attempted to review any applicable tax law and consulted with the CPA firm to ascertain what returns were being filed and what liability for certain taxes may exist, given the nature of the business and the types of purchases being made. Petitioner's arguments against the negligence penalty are largely based on the alleged inadequacies in the instructions for the return; however, even if the instructions did not provide enough guidance, Petitioner still failed to take any measures to ascertain if any use tax liability existed. Petitioner's claimed reliance on the instructions to the tax returns is not sufficient to establish that Petitioner exercised due care with respect to its use tax liability and the filing of its tax returns. Accordingly, the Tribunal finds that Petitioner has failed to establish reasonable cause for waiver of the 10% negligence penalty imposed under MCL 205.23(3).

Applicability of *Andrie*

At the close of the hearing, the parties were requested to brief the issue of whether or not the Court of Appeals decision in *Andrie* would apply to transactions involving purchases from

Michigan vendors. The Court of Appeals in *Andrie* ruled that the taxpayer was entitled to a presumption that the vendor paid the sales tax on the transaction that occurred in Michigan and the department did not rebut the presumption and, therefore, the transactions were not subject to use tax. Petitioner's argument that it is not liable for the use tax imposed in relation to purchases from eight Michigan vendors identified in its Post-Hearing Brief is premised on the determination made by the Court of Appeals. However, the Department of Treasury appealed that determination to the Michigan Supreme Court. In reversing the Court of Appeals' decision, the Michigan Supreme Court found that the burden was on the taxpayer to demonstrate it was entitled to the use tax exemption by showing that the sales tax was due and paid on the sale of tangible personal property. Specifically, the Michigan Supreme Court stated:

> The exemption statute unambiguously requires payment of the sales tax before it exempts the taxpayer from the use tax. It is not enough that the sales tax was due on the retail sale of the property; rather, sales tax must be both "due and paid" before the exemption applies. Thus, the department properly assessed use tax on in-state purchases where Andrie failed to submit evidence that sales tax was actually paid at the time of sale.

In the present case, Petitioner had failed to submit documentation during the audit that sales tax had been collected on certain purchases from the eight listed Michigan vendors, and Petitioner has not submitted any information or documentation to the Tribunal that would establish that sales tax had been collected. Accordingly, Petitioner is liable for the corresponding use tax on these purchases contained in the audit (as revised by the parties) for the tax periods at issue.

JUDGMENT

The Tribunal finds, based upon the Findings of Fact and the Conclusions of Law set forth herein, that Petitioner has failed to establish reasonable cause for waiver of the negligence penalty. Further, the recent Michigan Supreme Court's decision in *Andrie* precludes any further reduction in the use tax, as Petitioner has failed to provide proof that the sales tax had been paid. However, Petitioner is not liable for the use tax imposed for the 2003 and 2004 tax periods, as Petitioner did file a combined Sales, Use, and Withholding tax return for those years, and under MCL 205.27a(13), this constitutes a filing of a return sufficient to start the running of the 4-year period of limitations on assessments. As a result, the total use tax due under the assessment, based on the agreed upon revisions to the audit by the parties and the removal of the amount of

tax assessed for 2003 and 2004, is $141,495, with a negligence penalty of $14,150, and interest to be computed in accordance with 1941 PA 122. In correcting its records to reflect this Tribunal's decision, Respondent shall also reduce the amount of tax, penalty, and interest by application of Petitioner's payment of $99,002 on October 8, 2010, and any other payments Petitioner may have made with respect to this assessment.

IT IS SO ORDERED.

IT IS FURTHER ORDERED that Assessment Number S257356 is MODIFIED to reflect a total tax due (absent any payments made by Petitioner) of $141,495. The corresponding negligence penalty is $14,150, and the applicable interest is to be computed as provided by 1941 PA 122.

IT IS FURTHER ORDERED that Respondent shall cause its records to be corrected to reflect the taxes, interest, and penalties within 20 days of entry of this Final Opinion and Judgment.

IT IS FURTHER ORDERED that Respondent shall collect the affected taxes, interest, and penalties or issue a refund as required by this Opinion within 28 days of entry of this Final Opinion and Judgment.

This Opinion resolves the last pending claim and closes the case.

Steven H. Lasher

Entered: July 31, 2014
klm