STATE OF MICHIGAN
DEPARTMENT OF LABOR & ECONOMIC GROWTH
MICHIGAN TAX TRIBUNAL
NONPROPERTY TAX APPEAL

Genesys Group Ltd.,
Petitioner,

v

MTT Docket Nos. 316458 and 290394

Michigan Department of Treasury,
Respondent.

Tribunal Judge Presiding
Rachel J. Asbury
Susan Grimes Munsell

FINAL OPINION AND JUDGMENT

INTRODUCTION

Petitioner appeals Respondent's Decision and Order of Determination dated May 17, 2005, finding Petitioner liable, as assessed pursuant to Final Assessment J211111, for single business tax for the 1993, 1994, 1995, 1996, and 1997 tax years. Petitioner filed a separate petition on May 29, 2002, appealing Respondent's Intent to Assess J211111, dated April 2, 2002, for single business tax and use tax for the 1993, 1994, 1995, 1996, and 1997 tax years. The petitions were consolidated and a hearing in this consolidated matter was held on August 14 and 15, 2007. Petitioner was represented by Mark C. Pierce, Pierce, Duke, Farrell & Tafelski, PLC. Respondent was represented by Mark A. Meyer, Assistant Attorney General.

BACKGROUND

In MTT Docket No. 290394, Petitioner appeals Respondent's Decision and Order of Determination issued May 13, 2002, and Final Assessment J211111, dated April 2, 2002. On May 8, 2003, the parties filed a joint stipulation to place the matter in abeyance pending an

informal hearing and resultant Decision and Order of Determination. The Tribunal entered an order granting the joint motion and placed the case in abeyance. Respondent's status report dated May 17, 2005, stated that an informal conference had been held but no Decision and Order of Determination had been issued. On May 7, 2008, both parties filed status reports. Respondent stated that a Decision and Order of Determination had been issued and the case should be taken out of abeyance. Petitioner asserted that MTT Docket No. 316458 involved the same parties and the same assessment and the cases should be consolidated. On June 25, 2008, the Tribunal entered an order consolidating MTT Docket Nos. 290394 and 316458.

In MTT Docket No. 316458, Petitioner appeals Respondent's Decision and Order of Determination issued May 17, 2005, finding Petitioner liable for unpaid single business tax for the 1993, 1994, 1995, 1996, and 1997 tax years pursuant to Intent to Assess J211111. Petitioner did not pay the assessment and filed this appeal. The final assessment, J211111, for Michigan single business tax due is as follows,

Assessment	Tax Due	Interest*	Penalty
J211111	$1,376,173	*	$493,449

*Interest accruing and to be computed in accordance with sections 23 and 24 of 1941 PA 122.

PETITIONER'S CONTENTIONS

Petitioner offered the following proposed exhibits:

- P-1 Bankruptcy Confirmation Order
- P-2 2001 SBT Return filed by SES
- P-3 Purchase Agreement - SES
- P-4 All tax returns filed by Genesys Group, Ltd, including 1993, 1994, 1995, and 1996
- P-5 Audit Report conducted by the State of Michigan with attachments
- P-6 Recalculation of Correct Single Business Tax
- P-7 Curriculum Vitae of Michael Bozimowski
- P-8 Correspondence dated February 3, 1997 from Ernst & Young to Edward W. Fisher at Simplified Employment Services

P-9 Genesys Group Employee Management Services Agreement dated October 21, 1996
P-10 Genesys Group Service Agreement dated June 29, 1994
P-11 Genesys Group Staff Leasing Agreement dated July 23, 1993

The parties stipulated to the admission of Petitioner's exhibits 1, and 4 through 8. Petitioner's exhibits 9, 10, and 11 were exchanged after the initial exhibit lists were filed. The parties stipulated at hearing to the admission of these exhibits. Respondent objected to Petitioner's exhibit 3 as not relevant stating it "does not pertain to Genesys Group at all. Genesys Group doesn't appear anywhere . . .[i]t occurred after the tax years that are at issue here."[1] The Tribunal allowed the exhibit for informational purposes, the credibility of which would be weighed in the final determination of this matter.

Petitioner asserts that Genesys Group Ltd. and all of its successors, whether under the Genesys name or otherwise, are professional employer organizations.[2] Petitioner states that "Genesys Group, Ltd. ceased to be an operating company sometime in 1996. Other entities, some of which were doing business under an assumed name of Genesys continued the business until 1999, when all of the Genesys and Genesys-related entities were sold. As part of the sales agreement, SES, the purchaser, agreed to pay any taxes that were owing."[3]

Petitioner contends that, for the tax years at issue, payroll related to entities in a professional employer organization arrangement were included in the tax base of the entity that was the "true common law employer."[4] The determination of which entity was the true common law employer is based on the facts and circumstances of the specific arrangements. In the instant matter,

[1] Transcript page 82, ll 21-25
[2] Petitioner's prehearing statement, attachment
[3] Petitioner's prehearing statement, attachment
[4] Petitioner's prehearing statement, attachment letter from Ernst & Young

Petitioner asserts that payroll must be included in tax base of the subscribers to its services, not in Petitioner's tax base.

Petitioner argues that to determine who is the common law employer, the "primary inquiry is on who has the right to hire and fire, who has the right to control and direct the performance of the work."[5] Petitioner states that the "real area of inquiry here is who is it that gets the benefit of services that are performed . . . because . . . the single business tax is a value added tax, not an income tax."[6] Petitioner asserts that it performs a payroll function that included, in addition to the handling of wages, receiving "group discounts for insurance, for other benefits"[7] which allowed its subscribers, multiple small companies, to be more competitive with larger employers.

Petitioner offered the testimony of Mr. Craig Vanderburg. Mr. Vanderburg testified that he started Petitioner in early 1992. He testified that

> Genesys was in the business of providing outsourced human resource functions for its clients . . . in the areas of payroll administration, employee benefit administration, Workers' Compensation and safety compliance, HR consulting and a variety of issues associated with those primary functions.[8]

Mr. Vanderburg testified that the benefit he offered potential customers was "to outsource functions of your business that weren't core to operating a company"[9] including a variety of payroll related functions, such as withholding that allowed clients to eliminate the expense of administering those functions themselves. Petitioner could also negotiate with Workers' Compensation and health, dental, and vision care insurance providers and enhance the

[5] Transcript page 9, ll 22-24
[6] Transcript page 10, ll 4-9
[7] Transcript page 10, ll 21-22
[8] Transcript page 33, ll 17-23
[9] Transcript page 34, ll11-12

purchasing power of its clients by aggregating all of the companies they serviced. Petitioner charged a fee for this service.

Mr. Vanderburg testified that the Employee Management Service Agreement executed October 21, 1996,[10] the Service Agreement executed June 29, 1994,[11] and the Staff Leasing Agreement executed July 23, 1993,[12] were all forms and contracts used by Genesys for 1993, 1994, and 1995, however,

> [w]e never sold our clients any idea of providing them labor, we never sold our clients any idea of hiring or firing their employees and . . . we had no expertise in hiring or firing a shop worker or a pizza delivery boy, . . . [t]he last thing our clients would want us to do is make the determination of when to hire or fire people to run their business.[13]

Mr. Vanderburg testified that Petitioner did not set the wages of the employees of its customers, set hours of employment, or evaluate employee performance. Clients provided Petitioner with "their current internal payroll report"[14] which included current pay structure, all withholding information, and deductions. Petitioner would "merely take that data and pop it into our software system."[15]

Mr. Vanderburg testified that the wages for clients' employees were based on hours and wage information sent or faxed by clients to Petitioner's payroll department. Petitioner's payroll department would "process the payroll for [each] location based on the data they provided and . . . we would send out paychecks, payroll reports and an invoice to the client in the form of

[10] Petitioner's exhibit 9
[11] Petitioner's exhibit 10
[12] Petitioner's exhibit 11
[13] Transcript page 40, ll 12-20
[14] Transcript page 42, ll 3-4
[15] Transcript page 42, ll 8-9

overnight delivery."[16] The client distributed the paychecks to employees. Petitioner used either an "automated debit transaction out of the client's account"[17] to pay the payroll or Petitioner would deliver the payroll checks to the client and be paid upon delivery. Petitioner had "no obligation"[18] to pay the employees if the client did not pay Petitioner. Petitioner billed a service fee "which would include the markup of burden associated with payroll. . . . matching tax contributions for social security, unemployment costs, Workers' Compensation premium costs and then if we had employees at a location that did have health benefits, . . . premiums."[19] Petitioner had no discretion as to the amounts paid. Mr. Vanderburg further testified that payroll checks for some clients had the client name embossed if the client chose that service. Petitioner did have discretion in choosing insurance providers that it offered. Clients had the option to enroll.

Mr. Vanderburg testified that Petitioner did not provide any tools or equipment to customers' employees[20] and did not advertise for employees[21] for customers. He testified further that Petitioner did not have the "authority to direct an employee as to which facility he would work at"[22] if a client had multiple sites.

Mr. Vanderburg testified that by early 1997, Petitioner had ceased to exist. Mr. Vanderburg explained that "we restructured the entities so that they were put into a variety of different risk

[16] Transcript page 44, l 22-page 45, l 3
[17] Transcript page 45, ll 24-25
[18] Transcript page 46, l 13
[19] Transcript page 46, l 24-page 47, l6
[20] Transcript page 50, ll 11-13
[21] Transcript page 50, ll 14-16
[22] Transcript page 50, ll 22-24

pools"[23] because "the number of clients and their employees put us in a position where our risks were growing"[24] and one program would no longer fit all clients. Mr. Vanderburg testified that "we had to create these pool . . . in separate entities."[25]

Mr. Vanderburg was asked to identify a Power of Attorney contained in Respondent's audit report.[26] Mr. Vanderburg testified that the signature on the Power of Attorney was not his and that the handwritten date was not his handwriting.[27]

On cross examination, Respondent asked Mr. Vanderburg to identify all of the following:

1. Petitioner's 1993 Michigan Annual Report on which he was listed as president.[28]
2. Petitioner's 1994 Michigan Annual Report on which he was listed as president[29]
3. Petitioner's 1995 Michigan Annual Report on which he was listed as president,[30]
4. Petitioner's 1996 Michigan Annual Report on which he was listed as president,[31]
5. Petitioner's 1997 Michigan Annual Report on which he was listed as president.[32]
6. Petitioner's 1998 Michigan Annual Report,[33] 1999 Michigan Annual Report,[34] and 2000 Michigan Annual Report on which Mr. Vanderburg was listed as president, secretary, treasurer, and director and on which Mr. Vanderburg's name, as resident agent, was crossed through.
7. Petitioner's 1993 U.S. Corporation Income Tax Return,[35]
8. Petitioner's 1994 Single Business Tax Return,[36] and
9. Petitioner's 1995 U.S. Corporation Income Tax Return,[37] all of which Mr. Vanderburg testified he believed bore his signature.

Respondent asked Mr. Vanderburg to read the following excerpts from an Employee Management Service Agreement,[38]

[23] Transcript page 53, l 25-page 54, l 2
[24] Transcript page 55, ll 15-16
[25] Transcript page 56, ll 11-22
[26] Petitioner's exhibit 5
[27] Transcript page 101, ll 12-21
[28] Respondent's exhibit 1
[29] Respondent's exhibit 2
[30] Respondent's exhibit 3
[31] Respondent's exhibit 4
[32] Respondent's exhibit 5
[33] Respondent's exhibit 6
[34] Respondent's exhibit 7
[35] Respondent's exhibit 16
[36] Respondent's exhibit 19
[37] Respondent's exhibit 20

> Client shall pay to Genesys all costs incurred by Genesys in connection with the leased employee, including but not limited to all payroll inclusive of bonuses and special payments, all applicable federal, state and local taxes, all premiums and contributions in connection with employee benefits, all insurance, . . . all Workers' Compensation premiums including required deposits, all unemployment compensation charges and all payments in connection with all pension retirement plans.[39]
>
> Paragraph 3.10: Genesys to terminate or lay off any leased employee assigned to client under any agreement,[40] the client would reimburse Petitioner for out of pocket expenses and terminate the employees.
>
> Paragraph 8.2: Genesys is an independent contractor of client and neither party is an agent of the other.[41]

Respondent asked Mr. Vanderburg to read the following excerpts from of the Service Agreement,[42]

> Paragraph 4: Recipient acknowledges that Genesys employs the workers covered by this agreement and which are assigned to the recipient's workplace.[43]
>
> Paragraph 9: Additionally, recipient acknowledges the fact that Genesys provides Workers' Compensation coverage to Genesys employees only and recipient is responsible for such coverage at recipient's work site for non-Genesys employees.[44]
>
> Paragraph 10: Recipient acknowledges that with respect to the Americans With Disabilities Act, Genesys' sole responsibility shall be as an employer hereunder.[45]
>
> Paragraph 18: Upon termination [of the Service Agreement], Genesys will immediately notify its employees assigned to recipient of the fact of termination of the contract and Genesys reserves the right to offer transfers to each employee upon termination.[46]

And from the Staff Leasing Agreement of Genesys,[47]

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[38] Petitioner's exhibit 9
[39] Transcript page 114, ll 13-24
[40] Transcript page 115, ll 8-10
[41] Transcript page 116, ll2-4
[42] Petitioner's exhibit 10
[43] Transcript page 117, ll 13-15
[44] Transcript page 117, l 25-page 118, l 4
[45] Transcript page 118, ll 9-12
[46] Transcript page 119, ll 6-10
[47] Petitioner's exhibit 11

> Paragraph 4: Recipient acknowledges that Genesys employs the workers covered under this agreement and which are assigned to recipient's workplace and that Genesys has entered or will enter into written employment contractual relationships with the workers so assigned.[48]
>
> Paragraph 8: Genesys retains a right of direction and control over aspects of work site locations to which leased employees are assigned which relate to the management and safety and risk in those locations.[49]

Mr. Vanderburg acknowledged signing Petitioner's exhibits 10 and 11 as president.

Mr. Vanderburg testified that when money was received from clients, that money was deposited in ". . . a Genesys corporate account."[50] From that account, "money was allocated for its specific purposes, the payment of the client employees' wages, the payment of their taxes, the payment of their insurance premiums and then the balance, . . . was utilized for operating expenses."[51]

On redirect, Mr. Vanderburg clarified that Genesys did not "have any right to assign a customer's employee to drive a vehicle . . . [or] to assign any customer employee to any particular facility." [52] Mr. Vanderburg testified that if Genesys objected to where a particular employee was working, "we'd be terminated by the client. . . . As a matter of practice, we would never object to that."[53]

Petitioner offered the testimony of Michael D. Bozimowski,[54] who reviewed Respondent's audit and testified that in his opinion the audit contained errors. Mr. Bozimowski prepared a report that recalculated Petitioner's single business tax liability. Mr. Bozimowski further testified that, in his opinion, the audit reflected interpolated values that were derived from a methodology he

[48] Transcript page 121, ll 16-21
[49] Transcript page 122, ll 18-22
[50] Transcript page 129, ll 23-25
[51] Transcript page 130, ll 6-11
[52] Transcript page 152, l 20-page 153, l 6
[53] Transcript page 154, ll 6-10
[54] Mr. Bozimowski's CV is Petitioner's exhibit 7

characterized as "[n]ot reasonable."[55] Mr. Bozimowski stated that the audit included "two things that were slightly disturbing, one statement that says maybe this will give the taxpayer rise to take this seriously and then the other, . . . was, well, the lack of any communication with the taxpayer direct."[56]

Mr. Bozimowski testified that, in his opinion, based on his understanding of the contracts, his conversations with Mr. Vanderburg, and after reviewing all the records, "[i]t's the customer that gets the benefit"[57] of the client's employees. Mr. Bozimowski asserted that for purposes of the single business tax, you look to the value added to determine "whose employees were they before this service company came in."[58] Mr. Bozimowski testified that Petitioner was required, for Internal Revenue Service purposes, to use the word employer but "an issue as to whether or not these even were wages [to be included in Petitioner's tax base] for SBT purposes"[59] was a separate issue.

On cross-examination Mr. Bozimowski testified that he did not "provide any auditing services for Petitioner at any time."[60] Mr. Bozimowski was asked to review the $14,000,000 entry on Petitioner's 1993 tax return, Schedule A at line 2. Mr. Bozimowski testified that "[i]n talking to Mr. Vanderburg and in looking again – it represents those pass-through wages."[61] Mr. Bozimowski contended "that's the difference when the SBT says that your 940, 941's, although

[55] Transcript page 166, l 6
[56] Transcript page 168, ll 13-18
[57] Transcript page 174, l 3
[58] Transcript page 174, ll 8-9
[59] Transcript page 177, ll 18-19
[60] Transcript page 196, ll 21-24
[61] Transcript page 197, ll 18-19

prima facie evidence of being an employer, . . . are rebuttable . . . from a value-added point of view, we have the ability under Michigan law to . . . say but are you really getting that benefit."[62]

Respondent asked Mr. Bozimowski, "[w]asn't it the department's policy that employee wages were added back to the PEO?"[63] Mr. Bozimowski responded that as to employees of the PEO itself, those wages should be added back. As to wages of leased employees, "it was the Department's contention. . . that they would follow the 940, 941, and that those employees would be added back to the PEO."[64] Mr. Bozimowski admitted that Petitioner did not add back the wages of the leased employees.

RESPONDENT'S CONTENTIONS

Respondent offered the following proposed exhibits:

R-1 Michigan Annual Report Profit Corporations 1993
R-2 Michigan Annual Report Profit Corporations 1994
R-3 Michigan Annual Report Domestic Profit Corporations 1995
R-4 Michigan Annual Report Domestic Profit Corporations 1996
R-5 Michigan Annual Report Domestic Profit Corporations 1997
R-6 1998 Profit Corporation Information Update
R-7 1999 Profit Corporation Information Update
R-8 2000 Profit Corporation Information Update
R-9 DLEG Corporation Entity Details
R-10 DLEG Corporation Entity Documents
R-11 Genesys Group, Ltd. Audit Report
R-12 Genesys Group, Ltd. Single Business Tax Audit
R-13 Genesys Group, Ltd. SBT Audit Transmittal
R-14 Genesys Group, Ltd. SBT Audit Determination Letter
R-15 Audit Production Report 10/1/97 to 9/30/98 (sealed)
R-16 Genesys Group, Ltd. 1993 U.S. Corporation Income Tax Return
R-17 Genesys Group, Ltd. 1993 Single Business Tax Annual Return
R-18 Genesys Group, Ltd. 1994 U.S. Corporation Income Tax Return
R-19 Genesys Group, Ltd. 1994 Single Business Tax Annual Return
R-20 Genesys Group, Ltd. 1995 U.S. Corporation Income Tax Return

[62] Transcript page 198, ll 15-24
[63] Transcript page 205, ll 20-22
[64] Transcript page 206, ll 4-7

R-21 Genesys Group, Ltd. 1995 Single Business Tax Annual Return
R-22 Michigan Department of Treasury Decision and Order of Determination/Informal Conference Recommendation
R-23 STAR Account Profile 2/2/07
R-24 Petitioner's Answers to Respondent's First Set of Interrogatories and Requests for Production of Documents
R-25 Department of Treasury Tax Audit Questionnaire, Genesys Group, Ltd.

The parties stipulated to the admission of all of Respondent's exhibits. The Tribunal finds, after review of Respondent's exhibit 15, that the exhibit must be sealed to avoid violating the confidentiality restrictions under MCL 205.28f as it contains information that identifies taxpayers other than Petitioner.

Respondent contends that Petitioner is the common law employer of the employees it provided to its clients. As such, Petitioner was required to add back to its tax base, as compensation, what it claimed were pass-through wages paid on behalf of its clients. Respondent asserts that the definition of business income, which includes

> *the performance of services, . . . made or engaged in, or caused to be made or engaged in within this state,* whether in intrastate, interstate, or foreign commerce, *with the object of gain, benefit, or advantage, whether direct or indirect, to the taxpayer or to others*[65] (Emphasis in original)

encompasses Petitioner's activities. Respondent further asserts that under *Trinova Corp v Department of Treasury*, 433 Mich 141;445 NW2d 428 (1989), "value added" is synonymous with "business activity."[66]

Respondent asserts that to determine who is the actual employer for single business tax purposes, the two part test under *Mid America Mgmt Corp v Department of Treasury*[67] must be utilized. If

[65] Respondent's brief, page 3
[66] Respondent's brief, page 3
[67] 153 Mich App 446; 395 NW2d 702 (1986)

an entity is required to withhold for federal income purposes, that person is "prima facie deemed an . . . employer."[68] This presumption may be rebutted by determining who has the ultimate control in the employee/employer relationship. If a contractual agreement exists, the plain and unambiguous language of the contract controls. Respondent asserts that Petitioner withheld from the leased employees for federal income tax purposes and, despite Mr. Vanderburg's testimony to the contrary, the contracts involved are clear and unambiguous in supporting a finding that, for single business tax purposes, the employees were Petitioner's.

Respondent offered the testimony of Rene Katlein, senior auditor for Respondent. Ms. Katlein conducted the audit of Petitioner. Ms. Katlein testified that she began the audit on May 8, 1998, and submitted it for review to her supervisor on June 29, 1998. The tax audit questionnaire[69] she was given listed Mr. Earl Belger as the contact person for Petitioner, was stamped as received by Department of Treasury on January 27, 1997, and was signed by Vipa Thanyakarn, Controller. The questionnaire stated "we have all records since business started." Ms. Katlein testified that the audit was conducted at Mr. Belger's office and that she met with him and spoke to him on the phone several times. Ms. Katlein testified that Mr. Belger provided her with the "1993, 1994, Federal 1120 returns, the 1993, 1994 SBT returns, income statements for 1993 [and] 1994."[70] She testified that she did not get a copy of Petitioner's 1996 federal income tax return. Ms. Katlein identified the audit report prepared at the conclusion of the audit[71]and submitted on June 29, 1998, which summarized the audit, the SBT transmittal letter, which described her audit and

[68] Respondent's brief, page 5
[69] Respondent's exhibit 25
[70] Transcript page 233, ll 4-6
[71] Respondent's exhibit 11

the records reviewed,[72] an audit determination letter stating the taxpayer had the opportunity to agree or disagree with findings,[73] an audit production report which listed audits she performed from October 1997 through September 3, 1997 on which Petitioner was listed and which included the notation that she had worked 50 hours on the audit,[74] and her audit work papers.[75]

Ms. Katlein testified that standard audit procedure would be

> basically . . . audit to the federal return, so I would use the federal return and see how it related to what they reported on the SBT returns. . . . go by the SBT return item by item, like gross receipts, business income, compensation.[76]

Ms. Katlein testified that Petitioner's gross receipts as reported on its federal returns for 1993, 1994, and 1995 matched its gross receipts reported for single business tax purposes. Ms. Katlein testified that Respondent generally requests 940's and 941's and "also look at the federal wages and do a reconciliation of wages with those records."[77] Ms. Katlein testified that she relied on the 1120's to estimate wages as no 940's or 941's were provided. Ms. Katlein used gross receipts information from 1993, 1994, and 1995 to project an expected increase for 1996, which she applied to determine 1996 gross receipts. She did a similar projection for the two months of 1997.

Ms. Katlein testified that for the tax years at issue,

> the Department's policy in terms of reporting . . . employee wages for a professional employer organization [was t]hat they would be wages of the employee leasing company unless they were officer salaries . . . and we would basically . . . find that out by looking at contracts [and] the IRS test, 20-point test.[78]

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[72] Respondent's exhibit 13
[73] Respondent's exhibit 14
[74] Respondent's exhibit 15
[75] Respondent's exhibit 12
[76] Transcript page 238, ll 8-13
[77] Transcript page 240, ll 12-13
[78] Transcript page 246, ll 5-12

Ms. Katlein testified that it was her opinion that the wages reported on Petitioner's federal returns were not reliable because "we like to look at Federal 940's and 941's also just to verify the wages . . . and I did not have those forms."[79] Ms. Katlein stated that she used the gross receipts method for her audit and that that method was more advantageous to Petitioner. Ms. Katlein answered affirmatively that she found that

> leased employee wages and associated costs were reported as direct costs under the cost of goods, sales section of [Petitioner's] return. . . . [o]n the income statements I was able to see what their cost breakdowns were and under that direct cost on the income statement it went into the wages and other benefits, payroll taxes. So that's where I associated the income statement and relayed them to the direct costs on the federal returns.[80]

Ms. Katlein testified that there was a meeting on May 14, 1998, at which no records were produced, a meeting was held on May 21, 1998, and the "last meeting was June 11th and then . . . presented your findings on June 19th."[81] Ms. Katlein agreed that she reviewed "some tax returns, some financial statements,"[82] and the audit was completed in 30 days. Ms. Katlein testified that she asked for 940's and 941's, which were not produced.

Ms. Katlein testified that her report contained the statement "[h]opefully at that time, additional records will be provided and an accurate deficiency can be determined."[83] Ms. Katlein agreed with the statement that the "deficiency that you determined is inaccurate"[84] with the qualification that it was inaccurate "because we did not receive all the records."[85] Although Ms. Katlein agreed that copies of contracts between Petitioner and clients would assist her "to see what the

[79] Transcript page 253, ll 8-11
[80] Transcript page 254, l 17-page 255, l 3
[81] Transcript page 266, ll 9-11
[82] Transcript page 268, ll 1-2
[83] Transcript page 288, ll 6-8
[84] Transcript page 288, ll 10-11
[85] Transcript page 288, l 12

relationship would be"[86] and that the "nature of that relationship determines how the single business tax is computed,"[87] she did not request copies of any contracts and she "wasn't supplied"[88] with independent evidence "that would determine one way or the other whether these customers' employees should actually be taxed to Genesys or to the real employers."[89]

FINDINGS OF FACT

The Tribunal's factual findings must be supported by competent, material and substantial evidence. *Antisdale v Galesburg*, 420 Mich 265; 362 NW2d 632 (1984). In that regard, the Tribunal finds that, subsequent to the issuance of the assessments herein appealed and after the conclusion of the hearing, Respondent adjusted its audit conclusions and assessments amounts as follows,

1. The single business tax liability for 1997 was zeroed out.
2. Gross receipts were changed for 1996 to agree with the 1996 federal 1120 return.
3. Business income for 1995 and 1996 were changed to agree with the federal 1120 returns.
4. Officers' wages were subtracted out for 1993, 1994, 1995, and 1996. (The 1995 cost of goods sold wages were an average of the 1993 and 1994 cost of goods sold wages.)
5. The apportionment percentage for 1993, 1994, 1995, and 1996 was changed to 93.3449%. This was determined using Petitioner's 87% sales apportionment percentage and 100% property and payroll factors.

As a result of these adjustments, Respondent's assessment as revised, "exclusive of statutory interest or penalties"[90] is as follows:

Assessment	Tax Due	Interest*	Penalty
J211111	$634,524	*	**

*Interest accruing and to be computed in accordance with sections 23 and 24 of 1941 PA 122.
**[91]

[86] Transcript page 294, l 24
[87] Transcript page 294, l 24-page 295, l 2
[88] Transcript page 296, l 7
[89] Transcript page 296, 3-7
[90] Respondent's post hearing brief, page 2

The Tribunal accepts the revisions made by Respondent. However, the Tribunal and both parties agree that these adjustments do not change the Tribunal's obligation to first answer the underlying, and possibly dispositive issue in this matter, whether compensation paid to the leased employees who work at client sites be included in Petitioner's tax base.

Respondent's Assessment is presumed to be valid. Respondent's position is that the salary of leased employees is included in the tax base of the employer. In support of that position, Respondent offered the testimony of its auditor who explained how she determined wages, and that, based on Respondent's policy, she then included those wages in Petitioner's tax bases.

It is undisputed that Petitioner was responsible for withholding for federal tax purposes based upon the payroll for all of its clients. Respondent offered copies of contracts and agreements that spelled out Petitioner's responsibilities and in which Petitioner was referred to as the employer of the client employees, which acknowledge that Genesys employs the workers covered by its leasing agreements and assigned to the clients' workplace, and provides for reimbursement to Petitioner if a sale or liquidation of a client's business causes Petitioner to terminate or lay-off leased employees. There was no evidence that the parties were unaware of the provisions of the contracts or that there was any duress related to the signing of the contracts. This establishes, *prima facie*, the presumption that Petitioner is the employer of all employees at all client sites. This presumption is, however, rebuttable and the burden shifts to Petitioner to overcome that

[91]Respondent did not provide the Tribunal with a recalculated penalty amount. While the auditor recommended a 50%, failure to file, penalty for tax years 1995 and 1996, it is unclear to the Tribunal at what percentage the penalty for tax years 1993 and 1994 was assessed as the total penalty related to the assessment was 39%.

presumption. Petitioner's burden of proof to establish that the Assessment is invalid or incorrect is difficult, but not insurmountable.

Based on the evidence presented and the testimony, the Tribunal finds Petitioner provided payroll services to nonrelated clients based on contractual arrangements with those clients. The Tribunal further finds that Petitioner established consolidated benefit programs, based on risk factors, and offered those benefit packages to its clients. Clients then chose whether to participate in the programs and offer benefits to its employees; Petitioner did not make that decision with regard to individual employees. This was offered to clients so that Petitioner's client companies could offer their employees benefit programs at rates below what would otherwise be available to the employees as individuals or to the individual client companies.

The business activities of the companies with which Petitioner had contracts were diverse and there was no evidence or testimony presented to support a finding that the client companies were in any way interconnected. When the agreements with Petitioner were entered into, all of its clients were existing, ongoing businesses and all had employees engaged in the work of the client company.

Some portions of the contracts that Respondent asked Mr. Vanderburg to read into the record contained clear statements that Petitioner was the employer. However, some of the portions read, and some that were not read, are contradictory and ambiguous making closer examination of the agreements appropriate. For example, although paragraph 3.10 of Employee Management

Service Agreement[92] stated "[i]n the event of the sale, dissolution, liquidation, reorganization or closing of client's business which causes Genesys to terminate or lay off any leased employee assigned to client under any agreement,"[93] that paragraph goes on to state, "client agrees to promptly reimburse Genesys out-of-pocket unemployment expenses and charges incurred by Genesys with respect to such employees." This second part of the sentence appears to place underlying responsibility for payment of unemployment expenses on the client although Genesys agrees to make the payments. Further, although the contracts and agreements, as read into the record, state

> Recipient acknowledges that Genesys employs the workers covered by this agreement and which are assigned to the recipient's workplace.[94]
>
> Upon termination, Genesys will immediately notify its employees assigned to recipient of the fact of termination of the contract and Genesys reserves the right to offer transfers to each employee upon termination.[95]
>
> Recipient acknowledges that Genesys employs the workers covered under this agreement and which are assigned to recipient's workplace and that Genesys has entered or will enter into written employment contractual relationships with the workers so assigned.[96]

No evidence or testimony of individual written contracts with any employee at a client site was provided or produced.

The Employee Management Service Agreement[97] begins by reciting that Petitioner is in the business of providing leased employees; the client is engaged in a business that

[92] Petitioner's exhibit 9
[93] Transcript page 115, ll 8-10
[94] Transcript page 117, ll 13-15
[95] Transcript page 119, ll 6-10
[96] Transcript page 121, ll 16-21
[97] Petitioner's exhibit 9

requires personnel; and Petitioner desires to lease employees to the client. Petitioner's responsibilities, to be provided based on a fee paid, are outlined as

a) Compilation, preparation and filing of all payroll and employee information
b) Making all property payroll deductions, and . . . payments . . . under local, State and Federal Laws
c) Administrative matters . . .
d) Secure and maintain insurance coverage
e) Furnish . . . workers compensation insurance covering the Leased Employees

Petitioner does not have the right or responsibility to hire, fire, manage, direct, place, set wages, or choose benefits. Petitioner's role is administrative.

These documents also contain the following provisions:

> Additionally, recipient acknowledges the fact that Genesys provides Workers' Compensation coverage to Genesys employees only and recipient is responsible for such coverage at recipient's work site for non-Genesys employees.[98]
>
> Genesys retains a right of direction and control over aspects of work site locations to which leased employees are assigned which relate to the management and safety and risk in those locations.[99]
>
> Client shall pay to Genesys all costs incurred by Genesys in connection with the leased employee, including but not limited to all payroll inclusive of bonuses and special payments, all applicable federal, state and local taxes, all premiums and contributions in connection with employee benefits, all insurance, . . . all Workers' Compensation premiums including required deposits, all unemployment compensation charges and all payments in connection with all pension retirement plans.[100]

In the first provision, it is not clear who are the Genesys employees at the client's work site and who are the non-Genesys employees. As to the second provision, Mr. Vanderburg testified that this related to safety and health aspects as required by the workers' compensation coverage.

[98] Transcript page 117, l 25-page 118, l 4
[99] Transcript page 122, ll 18-22
[100] Transcript page 114, ll 13-24

The Tribunal finds that the final provision, and Mr. Vanderburg's testimony at the hearing, reflect the true nature of the arrangements between Petitioner and its clients. Petitioner wrote checks and filed withholding for wages only as directed by its clients, based on payroll and documents provided by clients, benefit plans chosen exclusively by the client, at rates determined by clients, and only to the extent that those costs were reimbursed to Petitioner by its client. The employees were existing employees of the client when the contracts and agreements were entered into or employees subsequently hired by the client, not Petitioner. Petitioner did not advertise to fill client employee positions, interview potential employees, and had no independent obligation to pay any client employee. If a client did not pay Petitioner the amount of wages, benefits, and withholding represented by the checks written by Petitioner to be distributed by it clients, Petitioner did not write the checks and the employees were not paid.

In further analysis of the role of the parties to the agreements, the Tribunal reviewed the common law indicators of employee/employer relationships, the sample contracts submitted, the testimony and evidence submitted, and the relevant Michigan case law. As part of the audit report, Respondent's auditor included a list of client companies, and officers of those companies, the wages of whom were not included in Petitioner's tax base. In reviewing that list, and accepting the testimony that the list is indicative of Petitioner's client base, the Tribunal notes that the business of those clients is extremely diverse ranging from construction, to vending sales, to artists, to maintenance, to chiropractors, to engineering, and many more. The Tribunal does not find that Petitioner had the expertise to provide direct supervision to this varied and

dissimilar a group of employees. The Tribunal finds that competent and credible evidence and testimony support the following findings.

1. Petitioner's sole activity was to provide payroll management services and benefit program opportunities to client companies.
2. Clients with whom Petitioner contracted had existing employees when the contracts were entered into. The status of those employees did not change, in any substantive way, when the contract was executed.
3. Petitioner did not have the right to hire or fire client employees or set wages.
4. Petitioner did not have the right, or expertise, to direct the work of client employees.
5. Petitioner did not provide tools or equipment to the individuals who produced the work or determine which facility an employee would work at if there was a choice.
6. Petitioner did not set wages but used the payroll information provided to generate payroll checks. If a client did not provide adequate funds, Petitioner did not issue payroll checks.
7. Petitioner distributed payroll checks to clients who distributed the checks to the employees.

The Tribunal notes that Respondent elicited significant testimony from Mr. Vanderburg related to his signature on tax related documents. The Tribunal finds that testimony not to be relevant to the issue of Petitioner's responsibility for taxes at issue.

Petitioner asserts that "the lack of diligence by the Treasury Department is shocking and the positions taken by the Treasury Department are so lacking in factual support that the audit itself becomes worthless and unworthy of reliance."[101] The Tribunal finds that, based on the auditor's own testimony, there was less than a 30-ay period between first contact with the Petitioner's designated representative and the conclusion of her audit and presentation to her supervisor. The Tribunal further finds that Petitioner did not provide the auditor with relevant documents. Although the Tribunal may find troubling the auditor's statements indicating that her findings were not accurate, the time needed for each audit is individualized and comparison to the time taken in auditing other taxpayers is not a basis on which the Tribunal can make a determination in this matter. Even if the Tribunal were to find, which it does not, that the audit process in this

[101] Petitioner's post hearing brief page 4

matter could have been implemented in such a way as to assure a more complete or accurate result, these issues related to the audit process are not relevant to Petitioner's liability for the taxes herein at issue.

CONCLUSIONS OF LAW

Calculation of single business tax liability begins with business income, subject to statutory adjustments enumerated in MCL 208.9. One of those adjustments is the addition of compensation.[102] Compensation is defined for the tax years at issue as:

> Except as otherwise provided, . . . "compensation" means all wages, salaries, fees, bonuses, commissions, or other payments made in the taxable year on behalf of or for the benefit of employees, officers, or directors of the taxpayers and subject to or specifically exempt from withholding under chapter 24, sections 3401 to 3406 of the internal revenue code. ... MCL 208.4(3)

MCL 208.5 provided, for the tax years at issue:

> Sec. 5. (1) "Employee" means an employee as defined in section 3401(c) of the internal revenue code. A person from whom an employer is required to withhold for federal income tax purposes shall prima facie be deemed an employee.
> (2) "Employer" means an employer as defined in section 3401(d) of the internal revenue code. A person required to withhold for federal income tax purposes shall prima facie be deemed an employer.

IRS Publication 15-A and 26 CFR 31.3401(c)-1 provides some guidance for the tax years at issue in determining whether a person, who does not meet the general definition of employee under 26 USC 3401(c), is an employee based upon a common law employment relationship. 26 CFR 31.3401(c)-1(b) provides:

> (b) Generally the relationship of employer and employee exists when the person for whom services are performed has the right to control and direct the individual who performs the services, not only as to the result to be accomplished by the work but also as to the details and means by which that result is accomplished. That is, an employee is subject to the will and control of the employer not only as to what shall be done but how it shall be done. In this connection, it is not necessary that the employer actually direct or control the manner in which the services are performed; it is sufficient if he has the right to do so.

[102] MCL 208.9(5)

> The right to discharge is also an important factor indicating that the person possessing that right is an employer. Other factors characteristic of an employer, but not necessarily present in every case, are the furnishing of tools and the furnishing of a place to work to the individual who performs the services. In general, if an individual is subject to the control or direction of another merely as to the result to be accomplished by the work and not as to the means and methods for accomplishing the result, he is not an employee.
>
> . . .
>
> (d) Whether the relationship of employer and employee exists will in doubtful cases be determined upon an examination of the particular facts of each case.
>
> (e) If the relationship of employer and employee exists, the designation or description of the relationship by the parties as anything other than that of employer and employee is immaterial. Thus, if such relationship exists, it is of no consequence that the employee is designated as a partner, coadventurer, agent, independent contractor, or the like.

Generally, assessments issued by the Department of Treasury are presumed to be accurate and valid. It is the taxpayer's burden to demonstrate that the Department of Treasury's assessment is incorrect or invalid. Respondent establishes *prima facie* liability and Petitioner has the burden of going forward to overcome the rebuttable presumption of that liability and the accuracy and validity of the assessment.

The issue of whether compensation paid to a leased employee should be included in calculating the single business tax base of the lessee entity or the single business tax base of the leasing entity has been the subject of interpretation, litigation, and statutory amendment. See *Bandit Industries v Dep't of Treasury*, Docket. No. 99-17260-CM, unpublished opinion of the Court of Claims (September 7, 2000); *Herald Wholesale v Dep't of Treasury*, 262 Mich App 688; 687 NW2d 172 (2004); *BL Rentals, Inc v Dep't of Treasury*, unpublished per curiam opinion of the Court of Appeals, issued February 14, 2006 (Docket No. 257578). Prior to the Legislature's amendment of the definition of compensation in 2002, single business tax treatment of employee leasing companies was addressed by reference to the Internal Revenue Code, 26 USC 3401(c)

and (d), as construed and applied in *Mid-America Mgt Corp v Dep't of Treas*, 153 Mich App 446, 461; 395 NW2d 702 (1986). In applying a common-law test in that case, the Court cited with approval the Department's reliance on 26 CFR 3 1.3401 (c)(1) and (d)(1) which provided:

> Generally the relationship of employer and employee exists when the person for whom services are performed has the right to control and direct the individual who performs the services, not only as to the result to be accomplished by the work but also as to the details and means by which that result is accomplished. That is, an employee is subject to the will and control of the employer not only as to what shall be done but how it shall be done. In this connection, it is not necessary that the employer actually direct or control the manner in which the services are performed; it is sufficient if he has the right to do so. The right to discharge is also an important factor indicating that the person possessing that right is an employer. Other factors characteristic of an employer, but not necessarily present in every case, are the furnishing of tools and the furnishing of a place to work to the individual who performs the services. In general, if an individual is subject to the control or direction of another merely as to the result to be accomplished by the work and not as to the means and methods for accomplishing the result, he is not an employee.

Petitioner does withhold from the wages of all leased employees for federal tax purposes. This establishes a rebuttable presumption that Petitioner is the employer and wages must be included in its tax base. Respondent points out that the sample contracts[103] submitted as evidence contain language[104] which, on its face, lead to the conclusion that Petitioner was the employer. Some of the language relates to the management of safety, risk and labor matters for which Petitioner is responsible as the entity that carries the workers' compensation insurance. In other portions of the agreements, workers are referred to as Genesys employees. The Employee Leasing Agreement[105] submitted by Petitioner contains language reserving to Petitioner "the right to offer transfer to each of its employees upon termination."[106]

[103] Petitioner's exhibits 9, 10, and 11
[104] Respondent's post hearing brief pp 7-9
[105] Petitioner's exhibit 11
[106] Petitioner's exhibit 11 page 11

In *Herald Wholesale,*[107] the companies' agreement provided that Amstaff would be the employer of the employees it provided to plaintiff and would be responsible "for such administrative employment matters as payment of all federal, state and local employment taxes, providing workers' compensation coverage, as well as nonobligatory fringe benefit programs for its employees." The Court in that case found no basis for determining that the companies' intent, as expressed in their agreement, was other than for the purposes expressed. "In a multiparty transaction, this Court should honor the allocation of rights and duties effected by the parties in an agreement, when supported by tax-independent considerations."[108]

In this case, however, there was comprehensive testimony at the hearing by Mr. Vanderburg, Petitioner's president, regarding Petitioner's daily operations. This presented a view quite different than that portrayed by the contract language introduced by Respondent. And the contracts contain language that is equally supportive of Petitioner's position. That Petitioner and Respondent attach different, yet reasonable, meanings to the words of the contracts and agreements, indicates some level of ambiguity or uncertainty.

When two parties reduce their agreement to a writing that they agree is a complete and accurate statement of their agreement, extrinsic evidence of antecedent and contemporaneous understandings is inadmissible for the purpose of varying or contradicting the writing."[109] However "extrinsic evidence is admissible to resolve"[110] the threshold question of whether the parties intended the writing to be a complete expression of their agreement as to the matters

[107] *Herald Wholesale, Inc v Dep't of Treasury*, 262 Mich App 688; 687 NW2d 172 (2004)
[108] *Stratton-Cheeseman Mgt Co v Dep't of Treasury*, 159 Mich App 719, 725; 407 NW2d 398 (1987)
[109] *Van Penbrook v Zero Mfg Co*, 146 Mich App 87; 380 NW2d 60 (1985)
[110] *NAG Enterprises, Inc v All State Industries, Inc,* 407 Mich 407; 285 NW2d 770 (1979)

covered. Further, extrinsic evidence is not prohibited to "determine the actual intent of the parties."[111] Thus, the Tribunal concludes that it is appropriate to give consideration to Mr. Vanderburg's testimony as to this threshold question and regarding Petitioner's activities.

The agreements give Petitioner control over management of safety, risk, and labor matters but they do not give Petitioner exclusive control over the employees whose wages are at issue. The Tribunal finds credible Mr. Vanderburg testimony that Petitioner's control over safety, risk, and labor matters were based on workers' compensation and other benefit related considerations; that clients were solicited for the purpose of providing payroll management and to establish competitive risk pools for insurance; and that each client's payroll was prepared based on the information provided by the client of its employees and a check for each employee was given to the client employer to distribute. Mr. Vanderburg testified that Petitioner did not advertise for or hire employees for any client site, give direction to any employee at any client site, or visit client sites to oversee the work done or that they had the right to do so. No evidence or testimony to the contrary was provided. Based on the number, size, and type of Petitioner's clients, in order to direct the work of the employees involved, Petitioner would have had to have expertise in many unrelated technical fields and no evidence of that was provided.

The Court in *Mid America*[112] applied a very practical, fact-intensive test, which, in this case, Petitioner has met. In the instant matter, in no practical way did, or could, Petitioner direct any aspect of the work of the employees of its clients. Each client had complete control of the terms

[111] *Goodwin, Inc v Orson E. Coe Pontiac, Inc*, 392 Mich 195; 220 NW2d 664 (1974)
[112] *Mid-America Mgt Corp v Dep't of Treas*, 153 Mich App 446; 395 NW2d 702 (1986).

of employment, hours of employment, and work to be accomplished. Petitioner did not decide the customers that its clients worked for or provide the tools to do the work.

The Tribunal carefully reviewed the testimony and evidence, including the sample contacts provided, and took into consideration the circumstances and the substance of the matters under consideration, as well as the form of agreements offered.

The Tribunal concludes that Petitioner did not have the ultimate control over the employees in question necessary to establish that Petitioner was the employer. Petitioner provided reliable and credible evidence and testimony sufficient to rebut the presumption of liability based on Petitioner's withholding for federal tax purposes for the employees involved. Under the *Mid America*[113] test, Petitioner was not the employer and the compensation paid to employees should not have been added back into Petitioner's tax base.

The Tribunal concludes that the assessment against Petitioner should be cancelled. Having determined that the assessment against Petitioner should be cancelled the Tribunal does not recalculate, or require Respondent to recalculate, interest and penalty based upon Respondent's revised assessment. Further, the Tribunal does not make any determination regarding an appropriate apportionment factor.

Although both parties have interchanged Petitioner with Craig A. Vanderburg on pleadings and other documents in this matter, Respondent issued the challenged assessment against The Genesys Group, Ltd. The Tribunal had jurisdiction only over the appeal of that assessment and,

[113] *Mid-America Mgt Corp v Dep't of Treas*, 153 Mich App 446; 395 NW2d 702 (1986).

under this docket and based on the testimony and evidence presented at hearing, this decision is made only as to the liability of Petitioner, The Genesys Group, Ltd.

JUDGMENT

IT IS ORDERED that Assessment No. J211111 is CANCELLED.

This Opinion and Judgment resolves all pending claims in this matter and closes this case.

MICHIGAN TAX TRIBUNAL

Entered: February 24, 2010 By: Rachel Asbury