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

Farnell Contracting, Inc.,
Petitioner,

v

MTT Docket No. 15-003818

Michigan Department of Treasury,
Respondent.

Tribunal Judge Presiding
Preeti Gadola

FINAL OPINION AND JUDGMENT

INTRODUCTION

Petitioner, Farnell Contracting, Inc. ("Farnell"), appeals Final Assessment No. TY40398 levied by Respondent, Michigan Department of Treasury, on May 22, 2015. The Final Assessment established that Petitioner owes use tax in the amount of $217,050, plus interest in the amount of $49,597.54 for audit period March 1, 2008 to February 29, 2012.[1] Edward S. Kisscorni, Certified Public Accountant, represented Petitioner, and James A. Ziehmer, Assistant Attorney General, represented Respondent.

A hearing on this matter was held on May 25, 2016. Petitioner's witnesses were Douglas B. Farnell, President, Farnell Contracting, Kathleen M. Farnell, Treasurer, Farnell Contracting and Joyce M. King, Certified Public Accountant. Respondent's sole witness was Shaquanda Baylock, Auditor, Michigan Department of Treasury.

The Tribunal ordered the parties to submit post-hearing briefs and Petitioner filed its brief on June 28, 2016 and Respondent filed its brief on June 27, 2016. No response briefs were permitted.

Based on the evidence, testimony, the Tribunal finds Petitioner is in part a "contractor" liable for use tax and interest, and in part a "retailer."

PETITIONER'S CONTENTIONS

Petitioner contends it is a retailer and sells tangible personal property, in the form of cabinets, counter tops, wall shelves, desks, mail box cubbies, free standing shelving, tables, wall cabinets, rods, fume hoods, and cabinets on wheels, among other items. The items are sold,

[1] Interest continues to accrue per 1941 PA 122. Interest shown above is current as of the date of the assessment.

delivered or direct shipped, put in place and sometimes incidentally attached to realty in laboratories. Petitioner contends that in this matter, it sold tangible personal property to exempt institutions, who returned to it signed exemption certificates, which Petitioner was required to obtain by law.[2] As such, Petitioner was not obligated to collect sales tax and remit it to the state.[3] Petitioner denies, as Respondent contends, that it is a contractor affixing the furniture to realty, therefore, it does not incur use tax liability as a consumer in the business of constructing, altering, repairing or improving the real estate of others. It simply orders and supplies, as a factory representative, premanufactured laboratory furniture to exempt entities, without permanently affixing the items, including mechanicals, for which it is not licensed. It further removes the personal property laboratory furniture and equipment, remodels the laboratories and even relocates the furniture to other facilities as it is not affixed to realty and made a permanent part of the same.

There is also a contention that Respondent did not use source documents, or original records of a transaction, when computing the amount of use tax owed by Petitioner, but conducted an improper, indirect audit. Respondent admitted that it started with costs of goods sold ("COGS") from page one of Petitioner's tax returns, however Petitioner contends, upon meeting with it, Respondent subtracted items like auto reimbursement, machinery rental, licenses and permits from page two of the tax returns. After the informal conference, Respondent further reduced the amount of the assessment as a result of additional exempt transactions it found from Petitioner's documentation, however, had Respondent given it a complete list of jobs it rejected, it would have provided source documents regarding the rejected transactions, which would prove no tax was due.

Petitioner's finally contends it is not liable for any sales tax owed, if its customers improperly claimed exemptions pursuant to MCL 205.62(5), as the purchasers are liable for tax due under the statute.

PETITIONER'S ADMITTED EXHIBITS

P-1 Final Bill for Taxes Due

P-2 Notice of Preliminary Audit Determination

[2] The exempt institutions include municipalities, schools, colleges and universities. See MCL 205.62.
[3] In transactions where tangible personal property is sold to non-exempt entities by Petitioner, sales tax is collected and remitted.

P-3 Final Audit Determination Letter

P-4 Decision and Order of Determination

P-5 Use Tax Audit Report and Findings

P-6 Use Tax Audit Schedules

P-7 Henry Wagner, Supervisor – FAX

P-8 Transaction Detail by Account – January through December 2008

P-9 Transaction Detail by Account – January through December 2009

P-10 Transaction Detail by Account – January through December 2010

P-11 Transaction Detail by Account – January through December 2011

P-12 Transaction Detail by Account – January through December 2012

P-13 Trial Balance – 12 Months Ended December 31, 2008

P-14 Trial Balance – 12 Months Ended December 31, 2009

P-15 Trial Balance – 12 Months Ended December 31, 2010

P-16 Trial Balance – 12 Months Ended December 31, 2011

P-17 Trial Balance – 12 Months Ended December 31, 2012

P-18 Financial Statements – December 31, 2009 and 2008

P-19 Financial Statements – December 31, 2011 and 2012

P-20 Financial Statements – December 31, 2012 and 2011

P-21 Form 1120S – US Income Tax Return for an S Corporation – 2008

P-22 Form 1120S – US Income Tax Return for an S Corporation – 2009

P-23 Form 1120S – US Income Tax Return for an S Corporation – 2010

P-24 Form 1120S – US Income Tax Return for an S Corporation – 2011

P-25 Form 1120S – US Income Tax Return for an S Corporation – 2012

P-26 Laboratory Furniture by Category with Descriptions

P-26a Cabinets

P-26b Counter Top

P-26c Wall Shelves

P-26d Desk

P-26e Mail Boxes - Cubbies

P-26f Free Standing Shelving

P-26g Tables

P-26h Wall Cabinets

P-26i Rods

P-26j Fume Hoods

P-26k Cabinet on Wheels

P-27 Farnell Contracting – Profit and Loss by Job, March 2008 through February 2012

P-28 Farnell Contracting – Exemption Certificates, March 2008 through February 2012

P-29 Farnell Contracting – Exempt Material Purchases by Job and by Vendor, March 2008 through February 2012

P-30 Farnell Contracting – Exempt Retail Sales Spreadsheet – Material by Category, March 2008 through February 2012

P-31 Farnell Contracting – Documents from Job Files, March 2008 through February 2012

PETITIONER'S WITNESSES

Douglas B. Farnell

Douglas B. Farnell ("Mr. Farnell") is the President of Petitioner, Farnell Contracting, Inc. He testified the company sells laboratory furniture and equipment to schools, colleges and universities.[4] He testified the company performs any service required by the customer, including unloading the truck, distributing items, and unwrapping them, however, the company does not connect the furniture to building systems, as it does not have a state builder's license, mechanical /electrical licenses of any kind, nor does it have mechanical contractors, plumbers or electricians on staff.[5] Mr. Farnell testified the company does not manufacture furniture and that all furniture sold by it comes from various manufacturers across the country, for which Petitioner is a factory representative.

Mr. Farnell placed the items Petitioner sold, during the audit period, that it alleges were considered fixtures by the Department into eleven categories, put forth on a summary sheet, and described them by referring to photographs/drawings included as exhibits.[6] He testified regarding pre-manufactured metal cabinets that sit on the floor and are interconnected with

[4] Petitioner alleges tax exempt sales of cabinets, countertops, free-standing shelving, and wall cabinets were sold to municipalities. See P-30.
[5] Tr. at 18.
[6] See P-26, P-30.

screws to create an island. He contends the cabinets are secured to the wall with a screw or possibly a plastic anchor, but when laboratories are relocating they take the cabinets with them due to their high cost. The cabinets have common countertops, which Petitioner sells, and silicone lubricant or silicone caulking is utilized to attach the countertops to the cabinets so they're easily removable. The captions to the photographs state that neither the cabinets, countertops, nor the wall are damaged when the cabinet(s) and countertop(s) are removed.[7]

The third item Mr. Farnell discussed are wall shelves, which he testified are attached to each other and anchored to the wall so they don't fall over. He testified that the shelves are custom made, expensive and are relocatable. Petitioner also sells desks to laboratories which are utilized with stools or chairs to perform laboratory tasks. They may be secured to the wall, but most of the time are not attached to the floor or wall, then countertops are attached with silicone caulk. Again, removing the desks does not damage the desk or the realty. With regard to the desk in the photo, which shows gas and air fixtures, Mr. Farnell testified that loose fixtures can be provided, but not connected to gas or air sources by Petitioner, however, he does acknowledge that gas, electric and plumbing lines run through the desks.[8] He also testified that the desks sometimes have sinks which Petitioner delivers, but does not install or connect to plumbing.

The fifth item discussed are mailboxes or "cubbies," which sit on cabinets and are custom to the space. They are secured to the wall for safety purposes with an angled clip or screw and an anchor. The cubbies are easily removable and are not damaged when removed, nor is the real estate. Freestanding shelving are the next items described and are clipped together without tools, occasionally anchored to the wall, are easily removable and are not damaged nor do they damage the realty upon removal.[9]

The seventh item consists of tables, which are not anchored to anything and are on guides or wheels so they can be easily moved or rearranged. Mr. Farnell testified that tables are the most common item sold to schools and are sold in bulk. He further testified that Petitioner simply unloads the tables, attaches legs, wheels or guides and countertops and they're ready to go. The next item is premanufactured wall cabinets, which are anchored to the wall by screws

[7] Tr. at 20-21, 44. See Exhibits P-26a and P-26b.
[8] Tr. at 26-27, See Exhibit P-26c and P -26d.
[9] Tr. at 30-31, See Exhibits P-26e and P-26f.

and plastic anchors. Mr. Farnell testified they are easily removed, relocated, are not damaged and do not damage the realty when removed. [10]

Petitioner sold to its tax exempt customers, rods that are utilized with sockets and clamps to stabilize Bunsen Burners, beakers, and other types of glassware utilized in a laboratory. Petitioner generally hands them to the instructor, but sometimes hangs them to ensure an accurate count. The rods are not attached to the desks, but screwed into a socket that screws into the desk, and are movable between desks. The tenth item consists of fume hoods that sit on countertops and are not attached. They are utilized with filters or exhaust systems that are not supplied or connected by Petitioner. Other mechanical systems necessary for the operation of the hoods consist of plumbing, gas, air and electrical, all of which Petitioner is not licensed to complete. The fume hoods are utilized for experiments to vent gases, are easily removed and do not damage realty. The last items are cabinets on wheels which come in all different sizes and shapes and are clearly not attached to the realty in any manner.[11] In his testimony, Mr. Farnell also indicated that some items are secured by bolts.[12]

Mr. Farnell testified that Petitioner has the capability to move lab furniture and equipment and that laboratories are often expanding or relocating. He testified during a relocation, Petitioner picks up old equipment, transports it to the new lab and puts it back together again. He testified the company owns a 23 foot enclosed trailer to facilitate the relocation of the equipment and furniture. He testified that Petitioner often purchases additional furniture during a remodel.[13]

When undergoing the audit from Respondent, Mr. Farnell indicated he and his accountant, Ms. King, requested a list of jobs it rejected which were characterized as sales of tangible personal property to exempt institutions by Petitioner. Mr. Farnell testified that the reply given was that audit work papers do not list the taxable jobs. As such, he examined the complete list of 98 jobs provided to the auditor, performed during the audit period, to determine which of those jobs were rejected. The goal was to analyze the jobs provided and determine how the auditor came up with the $217,050 assessment. Mr. Farnell commenced with actual job-by-

[10] Tr. at 31-32. See Exhibits P-26g and P-26h.
[11] Tr. at 32-38, 45. See Exhibits P-26i – P26k, R-16 005.
[12] Tr. at 41.
[13] Tr. at 21, 24.

job profit and loss statements from QuickBooks accounting software, went to Transaction Detail by Account to pick up COGS, took worksheets, purchase orders, purchase invoices, sales orders, work orders, custom set-up drawings,[14] among other documents, for each purchaser from the job file, and placed each item sold into a category included on a summary sheet. In order to further identify what was sold to each customer, Mr. Farnell was able to examine his accounts payable to determine who the vendor was, for example, Durcon Laboratories makes countertops and BMC makes fume hoods. He also testified that Petitioner collected sales tax exemption certificates from all its purchasers and provided them as an exhibit.[15] Mr. Farnell located 50 jobs he concluded Treasury rejected as retail sales of tangible personal property to an exempt institution.

Mr. Farnell testified that the Department's auditor took some of her information in support of her position that Petitioner is a contractor from its website that was completed by his son when he was 17-18 years-old, and was cut and pasted from other websites. Mr. Farnell testified the website is inaccurate and outdated with regard to the services offered by Petitioner.[16]

Kathleen M. Farnell

Mrs. Farnell is the Treasurer of Farnell Contracting, Inc., and completes the company bookkeeping, banking and pays its sales tax liability on a monthly basis. Sales tax is not collected and paid for sales to exempt institutions who have provided an exemption certificate. All records regarding sales tax are maintained including the certificates. Petitioner utilized QuickBooks Accounting Software which keeps track of all purchase orders, purchase invoices, and cost of materials, separated into materials and freight, by date, month, year, and customer. The system keeps track of customers alphabetically, by job number, and purchase invoices are paid by the computer. Each customer is assigned a job number which keeps track of all jobs for that customer. Mrs. Farnell is able to retrieve data by job number, customer name or date. She testified that QuickBooks and paper records are kept in Farnell Contracting's office and she has never been visited by any Department employee that she is aware of, but she supplied all materials requested by the Department auditor to Farnell's accountant, Ms. King.[17]

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[14] Tr. at 136-150.
[15] Tr. at 120-155. See P-28.
[16] Tr. at 23-24.
[17] Tr. at 55-64.

Joyce M. King

Ms. King is a certified public accountant who prepares Petitioner's annual sales, use and withholding report, financial statements, and corporate tax return, among other documents. She assisted the Farnells with gathering data for the Department's audit and the audit occurred in her office. Initially, the Department assessed Petitioner for "close to $500,000, $451,733"[18] in use tax liability based on costs of goods sold taken from page one of the corporate tax returns, however, after meeting with Ms. King, subtracted out items from page two such as materials, labor, job supplies, machinery rental or auto reimbursements. As such, the tax liability was reduced by the Department to about "$245,000, $243,803."[19] After the Department's informal conference, where supplemental documents were supplied, additional jobs were determined to be nontaxable further reducing the Petitioner's tax liability to about "$217,000."[20]

Ms. King testified that the Department never gave Petitioner a list of jobs it rejected as sales of tangible personal property to exempt institutions, so she and Mr. Farnell, recreated the final tax due from the audit report. Ms. King determined that Respondent's auditor, Ms. Baylock, commenced with COGS from the annual income tax returns, gave credit for jobs she determined had no installation, multiplied the remainder by 6% to conclude in tax due on purchases, then backed into tax due for the audited periods, without detail from taxable jobs. Total tax due was based on $3,617,500 in purchases.[21]

RESPONDENT'S CONTENTIONS

Respondent contends that Petitioner is a contractor incurring use tax liability by installing laboratory equipment and furniture as fixtures to real estate. It alleges the fixtures, such as desks, mail cubbies, cabinets, fume hoods, and sinks, are intended to be permanent additions to the realty. Respondent contends that Petitioner erroneously indicated it was entitled to an exemption from the collection and remittance of sales tax as a retailer, when in fact it owed use tax as a consumer in the business of construction. Further, Petitioner likens itself a contractor by entering into installation contracts with its customers and even utilizes "contracting" in the name of the company, "Farnell Contracting." Respondent contends that it made information and

[18] Tr. at 93.
[19] Tr. at 94.
[20] *Id*.
[21] Tr. at 83-103.

document requests for job contracts, with and without installation, and actual COGS for the entire audit period that were not provided in full, and as such, it could only analyze documents provided for calculation of use tax liability. Respondent also contends it did analyze and review source documents, or documents provided directly by Petitioner, in its audit and backed out types of transactions that it determined were retail sales to tax exempt entities after discussion with the taxpayer and review of the additional relevant documents that were actually provided. Respondent also pulled from Petitioner's documentation to its summary sheet "complete plumbing rework" and faucets and sinks delivered by Petitioner, indicating that plumbing was completed by Petitioner.[22] Further, Petitioner's website put forth that "all mechanical connections" were provided,[23] confirming that Petitioner is a contractor.

RESPONDENT'S ADMITTED EXHIBITS

R-1 Corrected Intent to Assess
R-2 Audit Report and Findings
R-3 Supplemental Audit Report of Findings
R-4 Audit Schedules
R-5 IDR 9/27/12
R-6 IDR 10/9/12
R-7 IDR 10/22/12
R-8 Tax Audit Questionnaire
R-9 Taxpayer Questionnaire
R-10 Taxpayer Website
R-11 Sample Job Contract
R-12 Sample AIA Billing Document
R-13 Sample Sales Invoice
R-14 Sample Job Proposal
R-15 Comparison of Sales and Use Tax Bases
R-16 Photographs

[22] See R-31.6b and R-31.38
[23] See R-10.

RESPONDENT'S WITNESS

Shaquanda Baylock

Ms. Baylock is a Department Auditor who conducted the audit of Petitioner. She testified she determined Petitioner was a contractor who failed to pay use tax on its purchases of materials, but was charging its customers tax on the materials. She testified she determined Petitioner was a contractor acting as a retailer, which might be allowed if the amount of sales tax paid is greater than the amount of use tax due as a contractor,[24] however, that is not the case here. Ms. Baylock made an initial records request, did not receive everything she required, and sent three "IDRs" or information and document requests attempting to retrieve more materials. She testified that she did not receive all the documents she requested, for example she requested copies of all job contracts during the audit period and indicated she would stop by the office to copy them. She then narrowed her request to copies of all job contracts with installation and copies of all job contracts without installation. She did not request QuickBooks information, though she admitted it was likely the audit could be completed from Petitioner's QuickBooks entries.

Ms. Baylock testified she took the initial COGS from Petitioner's tax returns then subtracted out jobs she found to be exempt, after viewing the additional documents provided by Petitioner. She created a schedule of purchases she determined to be exempt sales and also subtracted hospital jobs, which are exempt for contractors. Finally, after subtracting retail sales and hospital jobs, she concluded in use tax liability. She did not, however, include specific details and supporting documents regarding the adjustments made after additional documents were provided, in the work file. Further, she reiterated, that she requested job contracts and supporting documents supplied as exhibits by Petitioner for this hearing, however, they were not provided to her at the time of audit or informal conference, so she computed tax due from the documents that were provided, the information gathered from Petitioner's website and from discussions with Petitioner.[25] Ms. Baylock testified that despite Mr. Farnell's testimony, that Petitioner did not install mechanicals or plumbing, Ms. Baylock found that it did.

[24] Tr. at 172 referring to Internal Policy Document 2005-3.
[25] Tr. 171-188; 199-201.

FINDINGS OF FACT

1. Petitioner sells and installs, laboratory furniture and equipment to/in institutions exempt from the payment of sales tax, such as government entities, schools, colleges and universities.
2. The furniture and equipment, including, cabinets, counter tops, wall shelves, desks, mail box cubbies, free standing shelving, wall cabinets, rods, and fume hoods, are attached to the real property by clips, screws, anchors and bolts to prevent them for separating from each other, moving or falling. Tables and cabinets on wheels are not affixed to realty.
3. Respondent conducted a use tax audit for the March 1, 2008 to February 29, 2012, tax periods.
4. The Final Audit Report indicated that Petitioner did not remit use tax during the audit period as required as it was a contractor engaged in the business of constructing, altering, repairing or improving the real estate of others. Petitioner also did not remit sales tax on the purchases of its customers of tangible personal property, if the customer supplied an exemption certificate, which Petitioner was required to collect and maintain by law. Petitioner did collect and maintain all exemption certificates provided by its customers.
5. The final audit assessed Petitioner with $243,803 in tax liability. Petitioner participated in an informal conference with the Department and upon conclusion of the conference, use tax liability was reduced to $217,050 based on additional documents provided, from which the Department concluded that some transactions, that were assessed use tax, were actually sales of tangible personal property, not affixed to realty, to exempt entities. Respondent's auditor did not keep a list of jobs rejected in the audit work file.
6. Petitioner filed an appeal with the Tribunal of the Department's Decision and Order of Determination finalizing the audit conclusion of $217,050 in use tax due.
7. For the appeal, Petitioner created a summary document supporting the jobs that were rejected by the Department as sales of tangible personal property to exempt institutions by analyzing its job contracts, including purchase orders, purchase invoices, bids, work orders and custom furniture placement and attachment diagrams and also reviewed vendor contracts and other relevant information gathered from its paper files and computer accounting program, QuickBooks, during the audit period.

8. The summary sheet puts forth $347,855 as the COGS, of tables during the audit period. The summary sheet puts forth $75,059 as the COGS of cabinets on wheels during the audit period.

CONCLUSIONS OF LAW

Petitioner's Motion for a Directed Verdict

At the close of its case in chief, Petitioner's representative requested the Tribunal direct a verdict in its favor. A directed verdict is defined as such, "A ruling by a trial judge taking a case from the jury because evidence will permit only one reasonable verdict."[26] In this matter, as explained to Petitioner's representative at hearing, there was no jury present, therefore, the Tribunal Judge could not, and cannot, take the case away from the jury. As such, the motion for a directed verdict is denied.

Is Petitioner a Contractor or a Retailer?

The first issue in this matter is whether Petitioner is a contractor for use tax purposes. If so, then it is a consumer of personal property that it affixed to real property and is subject to use tax on the purchase price of such property. On the other hand, if Petitioner is engaged in the business of making sales of tangible personal property at retail, it is subject to sales tax on sales to purchasers, unless an exemption applies.

Contractor is not defined by statute, however, Mich Admin Code, R. 205.71 provides guidance:

> (1) "Contractor" includes only prime, general, and subcontractors directly engaged in the business of constructing, altering, repairing, or improving real estate for others.
> (2) Contractors are consumers of the materials used by them. All sales to or purchases by contractors of tangible personal property are taxable, except when affixed and made a structural part of real estate for a qualified exempt nonprofit hospital or a nonprofit housing entity qualified as exempt under the sales and use tax acts.

The use tax act defines consumer in pertinent part:

[26] Black's Law Dictionary (10th ed).

> (g) "Consumer" means the person who has purchased tangible personal property or services for storage, use, or other consumption in this state and includes, but is not limited to, 1 or more of the following:
>
> **(i)** A person acquiring tangible personal property if engaged in the business of constructing, altering, repairing, or improving the real estate of others.[27]

"Sale at retail" is defined in MCL 205.51(1)(b) as "a sale, lease, or rental of tangible personal property for any purpose other than for resale, sublease, or subrent." Sales at retail are taxable under MCL 205.52(1)[28], unless exempt. MCL 205.54a(1)(a)[29] exempts sales to non-profit schools and MCL 205.54h[30] exempts sales to governmental agencies. Tangible personal property is defined in MCL 205.51a(q) as "personal property that can be seen, weighed, measured, felt, or touched or that is in any other manner perceptible to the senses . . . ."

The assessment at issue was imposed under the Use Tax Act, 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 of 6% of the price of the property. . . .[31]

For the following reasons, The Tribunal finds that Petitioner is in part a contractor in the business of "constructing, altering, repairing, or improving the real estate of others," by installing fixtures. "[I]tems which are found to be fixtures are considered to be part of the reality to which they are connected."[32] Petitioner is also in part a retailer, selling tangible personal property to exempt institutions. Both parties agreed at the hearing of this matter and in post-hearing briefs that the crux of this matter is a fixture analysis. Both parties agree that the legal test to be considered in determining whether the subject furniture and equipment are fixtures, is the three-prong test set by the Courts as put forth, below.

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[27] MCL 205.92(g)
[28] Except as provided in section 2a, there is levied upon and there shall be collected from all persons engaged in the business of making sales at retail, by which ownership of tangible personal property is transferred for consideration, an annual tax for the privilege of engaging in that business equal to 6% of the gross proceeds of the business, plus the penalty and interest if applicable as provided by law, less deductions allowed by this act.
[29] "A sale of tangible personal property not for resale to a nonprofit school, nonprofit hospital, or nonprofit home for the care and maintenance of children or aged persons operated by an entity of government,"
[30] "Sales to the United States, its unincorporated agencies and instrumentalities, any incorporated agency or instrumentality of the United States wholly owned by the United States or by a corporation wholly owned by the United States, the American Red Cross and its chapters and branches, and this state or its departments and institutions or any of its political subdivisions are exempt from the tax under this act."
[31] MCL 205.93(1)
[32] *Velmer v Baraga Area Schools*, 430 Mich 385, 394; 424 NW2d 770 (1988).

Michigan courts have considered a fixture analysis in numerous real property and non-property cases wherein the analysis is the same. The Court in *Michigan National Bank v City of Lansing*,[33] set forth the following tests in a published, real property case:

> The test to be applied in order to ascertain whether or not an item is a fixture emphasizes three factors:
> (1) Annexation to the realty, either actual or constructive;
> (2) Adaptation or application to the use or purpose of that part of the realty to which it is connected or appropriated; and
> (3) Intention to make the article a permanent accession to the realty. The intention which controls is that manifested by the objective, visible facts. The permanence required is not equated with perpetuity. It is sufficient if the item is intended to remain where affixed until worn out, until the purpose to which the realty is devoted is accomplished or until the item is superseded by another item more suitable for the purpose.

Michigan National involved drive through banking equipment, which was encased in cement, and in which canopies were built into place. The Court of Appeals found the equipment was permanently affixed and as such, were fixtures which were part of the real estate. Further, the Court found the items were adapted to the use of the realty because the present use of the building was dependent on the presence of the banking equipment, and the banking equipment could only be utilized when affixed to the realty. The Court in *Tuinier v Bedford Twp*., [34]applied the Michigan National test and determined that polyethylene greenhouses, which were "bolted in stubs embedded in concrete and attached to the realty by both bolts and gravity," were fixtures.[35] The Court found that the Tribunal mistakenly concluded that "petitioner did not intend to make the greenhouses permanent because petitioner had moved portions of the greenhouses, which could be severed from the real estate by removing the stub bolts and unhooking the utilities." [36] The Court reiterated the Michigan National test and stated, "the intent to make a structure permanent is not equated with an intent to make the structure last forever."[37]

In its post-hearing brief, Respondent cites, *Wayne Co v Britton Trust*,[38] wherein the Court discussed constructive annexation, first stating:

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[33] *Michigan National Bank v City of Lansing*, 96 Mich App 551; 293 NW2d 626 (1980)
[34] *Tuinier v Bedford Twp*, 235 Mich App 663; 599 NW2d116 (1999), a published opinion.
[35] *Id*.
[36] *Tuinier*, 235 Mich App at 671.
[37] *Id*. at 671-672.
[38]*Wayne Co v Britton Trust*, 454 Mich 608; 563 NW2d 674 (1988)

> "Annexation refers to
>
> the act of attaching or affixing personal property to real property and, as a general proposition, an object will not acquire the status of a fixture unless it is in some manner or means, *albeit slight,* attached or affixed, either actually or constructively, to the realty. That is, if the object is not attached to the land or to some structure or appliance which is attached to it, it will retain its character as personalty even though intended for permanent use on the premises." [Emphasis added][39]

The Court further stated, "[i]f an object is not physically affixed to realty, it may acquire the status of a fixture by constructive annexation."[40] The Court put forth its analysis of previous case law regarding constructive annexation in *Colton v. Michigan Lafayette Building,*[41] in which it found items such as repair parts to elevator switchboard, elevator rugs, window shades, awnings, double doors and trim, to be fixtures because "their removal from realty would impair both their value and the value of realty."[42] The Court concluded its rationale was similar to other jurisdictions, wherein, items that are part of or accessory to already annexed items, are constructively annexed to the realty. The Court considered objective facts to determine the intent of the party making annexation, not "secret subjective intent. Intent may be inferred from the nature of the article affixed, the purpose for which it was affixed, and the manner of annexation."[43]

Petitioner cites, *Granger Land Dev v Dep't of Treasury,*[44] in its post-hearing brief, which involved an exemption from Michigan's use tax for personal property used or consumed during industrial processing. The Court applied the same tests enumerated above and found the property tangible personal property and not a fixture. The property consisted of cells installed into a landfill and the Court reasoned,

> [T]here is no evidence that Granger erects the cells in order to improve the land or make it more valuable in and of itself; rather, Granger erects the cells to facilitate the processing of waste material into gas that it can sell to third parties. *Given these unique facts,* we conclude that Granger has

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[39] *Id* at 615, quoting 35 Am. Jur. 2d, Fixtures, § 5, p. 703. (emphasis added).
[40] *Id*.
[41] *Colton v. Michigan Lafayette Building*, 267 Mich 122; 255 NW 433 (1934).
[42] *Britton* at 616.
[43] *Id.* at 618-619. (internal citations omitted).
[44] *Granger Land Dev v Dep't of Treasury*, 286 Mich App 601; 780 NW2d 611 (2009).

> neither actually nor constructively attached the landfill cells to its real property.[45]

The Court reiterated a case by case analysis regarding the three tests set out above,

> Although there is no bright-line test for determining whether and when an item of personal property has become sufficiently connected with real property that it should be treated as part of the real estate, Michigan courts have traditionally examined all the relevant factors to determine on a case-by-case basis whether personal property has become sufficiently affixed to real property that it should be treated as a part of the real estate.[46]

The Tribunal finds the finding that each set of facts must be considered on a case-by-case basis to be apropos, however, finds the property in *Granger* to be too dissimilar to the items in this matter, to be of assistance. Further, the Court emphasized its fact specific conclusion, by pointing out the *unique set of facts* in that case.

Considering the laboratory furniture and equipment in this matter under the three tests characterized by the Courts above, the Tribunal finds the majority of the furniture and fixtures that are the subject of this matter, were installed as real estate fixtures, and after installation became a permanent structural component of the realty. As such, the Tribunal will consider Mr. Farnell's testimony and summary sheet, regarding the sorting of the rejected items, that were part of the rejected jobs, into eleven categories under the three prong fixture analysis, as it finds the testimony and summary sheet probative. The Tribunal is persuaded by Mr. Farnell, Mrs. Farnell, and Ms. King's testimony that the summary of eleven categories contains the furniture and equipment sold during the audit period in question, due to their careful and accurate accounting in QuickBooks and paper records.

1. Annexation to the realty, either actual or constructive

The Tribunal finds that nine categories of furniture and equipment on Petitioner's summary sheet, constitute fixtures, including the floor cabinets, countertops, wall shelves, desks, mail box cubbies, free standing shelving, wall cabinets, rods, and fume hoods, which are annexed to, or constructively annexed to, the realty. The floor cabinets are secured to the wall with a screw or plastic anchor, the wall shelves are anchored to the wall to prevent tip over, the

[45] *Granger*, 286 Mich App at 612-613. (emphasis added).
[46] *Id.* at 610-611. See also *Velmer*, 430 Mich App at 394.

desks may be secured to the wall, the mailbox cubbies are secured to the wall for safety purposes with an angled clip or screw and anchor, the "freestanding shelving" is attached to the wall, wall cabinets are hung on the wall with screws and sometimes anchors, and the Tribunal finds the fume hoods, countertops and rods to be constructively annexed to the realty as they are "part of or accessory to articles which are so annexed".[47] Countertops are clearly constructively annexed to realty as they are attached to floor cabinets and desks with silicone lubricant or caulk, rods are screwed into the desks with sockets, attached to holes predrilled by the manufacturer, and their only purpose is to be utilized with laboratory furniture, and fume hoods are an accessory to cabinets with countertops. Further, Mr. Farnell testified that some furniture was attached with bolts, and finally, at the other extreme, the Court in *Britton* considered the affixation could be slight.[48] As such the Tribunal finds the nine categories of property to meet test one regarding fixtures versus personalty. Further, although Petitioner testified that the removal of the items discussed above would not damage the articles or the realty, the Tribunal finds screw holes, clip and anchor damage to the walls and furniture would be left behind and as such meet the *Britton* test regarding fixtures as "their removal from realty would impair both their value and the value of realty."[49] The Tribunal opines, once removed from realty, the old fixtures may drop in value because they are outdated or damaged.

2. Adaptation or application to the use or purpose of that part off the realty to which it is connected or appropriated.

With regard to test two, the Tribunal finds the nine aforementioned categories found to be annexed or constructively annexed to realty, are also adapted to the use or purpose of that realty. Mr. Farnell testified that some of the categories, including wall shelves and mail cubbies are custom to the space, and the Tribunal finds others are clearly adapted to the purpose of a laboratory as they are affixed according to drawings and schematics developed by Farnell Contracting for the specific needs of the customer.[50] Pursuant to the *Michigan National* test, the laboratory furniture and equipment were adapted to the use of the realty because the present use of the laboratory was dependent on the presence of the laboratory furniture and equipment and

[47] *Britton,* 454 Mich at 618.
[48] *Id.* at 678-679.
[49] *Britton*, 454 Mich at 616.
[50] See P-31.

the laboratory furniture and equipment could not be utilized unless attached to realty for safety purposes or simply to keep items, such as wall cabinets, on the wall.[51]

3. Intention to make the article a permanent accession to the realty.

Again, although Petitioner testified it remodels and relocates laboratory furniture, the test is not if the furniture can be relocated, but is the intent, gleaned from objective facts, to make the articles a permanent accession to the realty? In this matter, the Tribunal finds the nine categories of property were meant to be permanently affixed as the items were attached to the walls, desks, or floor cabinets. Even though the laboratory equipment in this matter may be detached and moved like the greenhouses in *Tuinier*, the Court found the greenhouses to be fixtures because "[i]t is sufficient if the item is intended to remain where affixed until worn out, until the purpose to which the realty is devoted is accomplished or until the item has been superseded by another item more suitable for the purpose."[52] Here, it appears the nine items are affixed until remodeling is requested or required due to worn out, obsolete or insufficient furniture and equipment or until the purpose for which the realty is devoted, or its use as a laboratory, is accomplished. Further, Respondent also pulled from Petitioner's documentation to its summary sheet of completed jobs, "complete plumbing rework" and faucets and sinks delivered by Petitioner, indicating that plumbing was completed by Petitioner.[53] Also, Petitioner's website, despite Mr. Farnell's testimony that it is outdated, put forth that "all mechanical connections" were provided,[54] confirming Petitioner's intention to make the furniture and equipment a permanent accession to the realty. Finally, simply viewing photographs of the items in question confirms their affixation to the realty. The Tribunal queries how wall shelving and wall cabinets attached to walls are not fixtures?

With regard to Mr. Farnell's last two categories of equipment, the Tribunal finds tables and cabinets on wheels are not affixed, or constructively affixed, to the realty. Per Mr. Farnell's testimony, which the Tribunal finds persuasive, tables are not anchored to anything and are on guides or wheels so they can be easily moved or rearranged. Further, Petitioner simply unloads the tables, attaches legs, wheels or guides and countertops and they are ready for use. Mr. Farnell

[51] See *Michigan National*, *supra*.
[52] *Tuinier,* 235 Mich App at 671, quoting *Michigan National,* 96 Mich App at 554.
[53] See R-31.6b and R-31.38
[54] See R-10.

testified that tables are the most common item sold to schools and are sold in bulk. He also testified the cabinets on wheels, which come in all different sizes and shapes, are clearly not attached to the realty in any manner.[55]

In this matter, Petitioner was able to consider its QuickBooks records, paper job contracts, custom furniture placement diagrams, bids, purchase orders, work orders, vendor invoices and Mr. Farnell's, own recollection, to reconstruct jobs Respondent rejected as sales of laboratory furniture and equipment to exempt institutions. Originally 98 jobs were submitted and considered by Respondent, however, Respondent did not keep a list in its work papers with regard to which of the 98 jobs were rejected as sales of tangible personal property to exempt institutions, and Ms. Baylock did not recollect. The Tribunal is persuaded that Petitioner's summary of jobs performed during the audit period is accurate and complete, given its extensive software and paper filing system and finds the majority of the jobs rejected included the attachment of fixtures, subject to use tax. However, as noted above, the Tribunal finds Petitioner's tables and cabinets on wheels are not fixtures and as such Respondent's use tax assessment will be reduced by referencing their COGS in Petitioner's summary.

Petitioner cites several cases in its post-hearing brief that the Tribunal will address. It points to *Central Michigan Cementing Services LLC v Dep't of Treas*, [56] where the Court found, pursuant to *Granger*, that cement surrounding an oil and gas well is not meant to improve the land or make it more valuable, but to assist in the safe production of oil and natural gas. The drills are eventually removed and the wells are sealed, therefore the cement does not become a structural part of the real estate. The Tribunal finds the cement at issue in *Central Michigan Cementing* to be too dissimilar to the items in this matter as were the "cells" in *Granger*.

Petitioner further cites *West Shore Services, Inc. v Dep't of Treas*,[57] a use tax case, wherein the Court found outdoor warning sirens meant to alert the public of dangerous weather, to be fixtures attached to the real estate. The warning sirens are attached to fifty foot wooden poles, placed into holes in the ground with fill dirt surrounding them. Further, the poles can be

[55] Tr. at 31-32 37-38. See Exhibits P-26g, P26k.
[56] *Central Michigan Cementing Services, LLC v Dep't of Treas*, unpublished opinion per curiam of the Court of Appeals issued December 8, 2015 (Docket No. 323405). Michigan Court Rule 7.215(C)(1) provides that "[a]n unpublished opinion is not precedentially binding under the rule of stare decisis. Unpublished opinions should not be cited for propositions of law for which there is published authority."
[57] *West Shore Services, Inc. v Mich Dep't of Treas*, unpublished opinion per curiam of the Court of Appeals, issued July 21, 2015 (Docket No. 321085)

removed in under an hour using large industrial equipment and were designed to be easily removed. Once removal is complete, the ground is returned to the same condition it was in before installation. The Court found Petitioner took affirmative steps, including the use of heavy equipment, to affix the poles directly to the realty and as such they were fixtures subject to use tax. Petitioner distinguished the case before us because the size and weight of the laboratory furniture and equipment is too distinct from the property, and the Tribunal agrees, however, in *West Shore*, it should be noted, Petitioner took affirmative steps to affix the poles directly to the realty, as did Farnell, and they are "easily removed," such as the allegation in this matter.[58] Also, the Court in *Miedema Metal Bldg Systems, Inc v Dep't of Treasury*,[59] a use tax case, found that the grain bins were affixed to the real estate, even though they were merely bolted to the foundation.

Finally, Petitioner cites two Tribunal cases, *Dallman Industrial Corporation v Mich Dep't of Treas,*[60] and *Great Lakes West, LLC v Mich Dep't of Treas* ,[61] wherein the Tribunal found ATM kiosks, set in place and secured with bolts, not to be fixtures and commercial restaurant equipment sold to schools, colleges and universities procured, assembled, delivered and set in place, also not to be fixtures. In *Great Lakes*, Petitioner did not attach the restaurant equipment to the realty in any manner unlike the items here. Further, in *Great Lakes*, Petitioner did not create any plans or specifications for placement. In *Dallman*, Petitioner delivered, for a fee, ATM kiosks that were temporarily bolted, however, a contractor was subsequently hired to permanently affix the ATMs and provide electrical hook-up and dedicated circuits for the ATMs. In this case, Petitioner attaches the laboratory furniture and equipment permanently and no other contractor is required to provide further attachment. Further, it appears that in some instances mechanical installation services may be provided in this matter further evidencing affixation. The Tribunal also notes, in *Greystone International, Inc v Dep't of Treasury*,[62] the Tribunal found that theater seats bolted to the floor were affixed to real estate, even though they could be easily removed.

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[58] *Id.*
[59] *Miedema Metal Bldg Systems, Inc v Dep't of Treasury*, 127 Mich App 533; 338 NW2d 924 (1983).
[60] *Dallman Industrial Corp v Mich Dep't of Treas*, 23 MTT 36, (Docket No. 331862) issued June 6, 2011.
[61] *Great Lakes West, LLC v Mich Dep't of Treas*, 24 MTT 549, (Docket No. 418535) issued September 23, 2014.
[62] *Greystone International, Inc v Dep't of Treasury*, 25 MTT 210 (Docket No. 429973) issued May 10, 2013.

The Department's Audit

The second issue raised by Petitioner at the hearing of this matter, is the improper use by it of an alleged indirect audit. Pursuant to MCL 205.3(a):

> The state treasurer or a duly appointed agent of the state treasurer may examine the books, records, and papers touching the matter at issue of any person or taxpayer subject to any tax, unpaid account, or money the collection of which is charged to the department.

Indirect audit is defined under MCL 205.104a(7)(a) as,

> an audit method that involves the determination of tax liabilities through an analysis of a taxpayer's business activities using information from a range of sources beyond the taxpayer's declaration and formal books and records.

Petitioner alleges, pursuant to MCL 205.68(5), if it maintains sufficient records,[63] an indirect audit may not be performed:

> If a taxpayer has filed all the required returns and has maintained and preserved *sufficient records as required under this section,* the department shall not base a tax deficiency determination or assessment on any indirect audit procedure unless the department has a documented reason *to believe that any records maintained or returns filed are inaccurate or incomplete and that additional taxes are due.* [Emphasis added.]

Petitioner alleges that it has maintained and preserved sufficient records as required under this section, however, Ms. Baylock testified that she did not receive the documents she requested in her IDRs,[64] therefore the Tribunal finds she had reason to believe the records were incomplete. Further what constitutes sufficient records is defined by statute as "records that meet the department's need to determine the tax due under this act."[65] Also, pursuant to MCL 205.104a(4)(a) an indirect audit of books, records and papers is allowed: "The department may use an indirect method to test the accuracy of the taxpayer's books and records." Finally, in this matter, the Tribunal finds Respondent did not conduct an indirect audit, as it reviewed Petitioner's source documents provided, including any specific job information provided, to

[63]MCL 205.104a(7)(b) states, "'[s]ufficient records'" means records that meet the department's need to determine the tax due under this act."
[64] Tr. at 174-175.
[65] *Id.*

reduce the original tax assessment for additional jobs Respondent found exempt based on those records.

Had the Department conducted an indirect audit, again, there is no prohibition for the same.

Pursuant to MCL 205.104a(4):

> If a taxpayer fails to file a return or to maintain or preserve sufficient records as prescribed in this section, or the department has reason to believe that any records maintained or returns filed are inaccurate or incomplete and that additional taxes are due, the department may assess the amount of the tax due from the taxpayer based on an indirect audit procedure or any other information that is available or that may become available to the department. That assessment is considered prima facie correct for the purpose of this act and the burden of proof of refuting the assessment is upon the taxpayer.

Seller's Liability for Sales Tax

Petitioner contends that it is not liable for any sales tax owed because it properly collected and maintained exemption certificates from its customers, and if the customers were not in actuality, qualified for an exemption from the payment of sales tax, the customers, and not Petitioner are liable for the tax.

MCL 205.62[66] puts forth the reporting requirements regarding a seller of tangible personal property to an exempt institution:

> (1) If an exemption from the tax under this act is claimed, the seller shall obtain identifying information of the purchaser and the reason for claiming the exemption at the time of the purchase or at a later date.[67] The seller shall obtain the same information for a claimed exemption regardless of the medium in which the transaction occurred.
>
> (5) A seller who complies with the requirements of this section is not liable for the tax if a purchaser improperly claims an exemption. A purchaser who improperly claims an exemption is liable for the tax due under this act.

[66] Section 12 of the General Sales Tax Act.
[67] Section (7) relates to the later date requirement, but are irrelevant to this action as there is not contention that exemption certificates were not timely received.

There is no dispute that Petitioner obtained and maintained sales tax exemption certificates, however, the same is irrelevant, given in this matter, use tax is due by Petitioner as a contractor, not sales tax, regarding the items determined to be fixtures. Further, with regard to Petitioner's customers' alleged liability for sales tax, the Tribunal notes that the customers are not parties to this action.

JUDGMENT

IT IS ORDERED that Final Assessment TY40398 is MODIFIED. The assessment is reduced by $25,375 to $191,675 based on the COGS of Petitioner's tables and cabinets on wheels, not found to be fixtures by the Tribunal.

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

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

By Preeti P. Gadola

Entered: August 19, 2016

APPEAL RIGHTS

If you disagree with the final decision in this case, you may file a motion for reconsideration with the Tribunal or a claim of appeal with the Michigan Court of Appeals.

A Motion for reconsideration must be filed with the required filing fee within 21 days from the date of entry of the final decision.[68] Because the final decision closes the case, the motion cannot be filed through the Tribunal's web-based e-filing system; it must be filed by mail or personal service. The fee for the filing of such motions is $50.00 in the Entire Tribunal and

[68] See TTR 261 and 257.

$25.00 in the Small Claims Division, unless the Small Claims decision relates to the valuation of property and the property had a principal residence exemption of at least 50% at the time the petition was filed or the decision relates to the grant or denial of a poverty exemption and, if so, there is no filing fee.[69] A copy of the motion must be served on the opposing party by mail or personal service or by email if the opposing party agrees to electronic service, and proof demonstrating that service must be submitted with the motion.[70] Responses to motions for reconsideration are prohibited and there are no oral arguments unless otherwise ordered by the Tribunal.[71]

A claim of appeal must be filed with the appropriate filing fee. If the claim is filed within 21 days of the entry of the final decision, it is an "appeal by right." If the claim is filed more than 21 days after the entry of the final decision, it is an "appeal by leave."[72] A copy of the claim must be filed with the Tribunal with the filing fee required for certification of the record on appeal.[73] The fee for certification is $100.00 in both the Entire Tribunal and the Small Claims Division, unless no Small Claims fee is required.[74]

[69] See TTR 217 and 267.
[70] See TTR 261 and 225.
[71] See TTR 261 and 257.
[72] See MCL 205.753 and MCR 7.204.
[73] See TTR 213.
[74] See TTR 217 and 267.