STATE OF MICHIGAN

COURT OF APPEALS

NORTH AMERICAN BANCARD INC, Petitioner-Appellant,	UNPUBLISHED February 28, 2019
v	No. 344241 Tax Tribunal
DEPARTMENT OF TREASURY, Respondent-Appellee.	LC No. 16-003703-TT

Before: SWARTZLE, P.J., and MARKEY and RONAYNE KRAUSE, JJ.

PER CURIAM.

Petitioner North American Bancard, Inc (NAB) appeals by right the Tax Tribunal's denial of its request for a use tax refund. NAB provides credit card processing services, and as part of its business, it provides "terminals" to its customers. Most of the terminals are placed for free (and NAB retains ownership), but NAB also sells terminals outright. Most of NAB's customers are out of state. NAB initially paid use tax on the entirety of its terminals after an audit, but now seeks a refund, asserting that the terminals may not be taxed because some of them may be sold, and the terminals that leave the state may not be taxed because no taxable event occurs in Michigan. We affirm.

I. FACTS AND PROCEDURE

NAB is a provider of credit card and debit card processing services. NAB's customers are merchants, and NAB provides them with card readers or card processing terminals that communicate with NAB over a data line. NAB takes a percentage of each credit card transaction, and a third party performs the actual processing. Most of the terminals provided by NAB are "placed for free," meaning NAB retains ownership of the terminal, and the customer would be required to return it upon cancelling services or pay for any damage to the terminal. However, NAB also sells some of its terminals outright. All terminals are "locked" when deployed so the merchant would not be able to alter a terminal's programming or put it to other uses. However, if a merchant purchased a terminal outright, NAB would "unlock" the terminal upon request, whereupon the merchant could then use the terminal with other services.

NAB maintains its inventory of terminals at its headquarters in Troy. It has no way to track whether any particular terminal will eventually be sold or placed for free until the terminal is actually withdrawn from inventory for deployment. At that time, NAB programs it so that the merchant only needs to plug it in upon receipt. The terminals' programming was the same whether the terminal was placed for free or purchased, including terminals placed outside of Michigan. Approximately 90.13% of NAB's total equipment was deployed outside of Michigan. It was possible for merchants to provide their own equipment to use with NAB's services, although there was no evidence any merchants had ever done so. Similarly, it was possible for NAB to sell terminals without service agreements, but again, there was no evidence any such standalone purchases had ever occurred. Whether a terminal was sold or placed for free, NAB invoiced the terminal transactions separately from its service agreements.

According to NAB's tax manager, NAB's present policy was to self-assess use tax on the terminals and pay the tax as NAB purchased them. However, his predecessor had apparently not paid those taxes, which resulted in an audit by respondent. During the audit period, NAB deployed approximately $25 million worth of terminals, of which approximately $14 million worth of the terminals were returned during the same period. Some of those terminals, however, would eventually be redeployed. NAB had "revenue associated with" approximately $1.57 million worth of terminals, which would include terminals sold, but could also include payments by merchants for damaged placed-for-free terminals. NAB had no way to know why there was revenue associated with the terminals, such as whether it had been sold or whether NAB had been compensated for damage.

NAB does not contest that it owes use tax on terminals placed for free in Michigan. However, it contends that it does not owe use tax on any of the terminals deployed outside of Michigan, and that it should not pay any tax on any terminal until that terminal is withdrawn from inventory, because until that time every terminal has the potential to be sold. Respondent's position is that NAB is the consumer of the terminals, so it owes use tax at the time it purchases those terminals. The Tax Tribunal agreed with respondent, reasoning that even though NAB did sell some of its terminals, those sales were fundamentally intertwined with the sale of services, so NAB was not truly engaged in sales at retail. This appeal followed.

II. STANDARD OF REVIEW

"In the absence of fraud, review of a Tax Tribunal decision is limited to determining whether the tribunal erred in applying the law or adopted a wrong principle. The Tax Tribunal's factual findings are conclusive if supported by competent, material, and substantial evidence on the whole record." *Catalina Marketing Sales Corp v Dep't of Treasury*, 470 Mich 13, 18-19; 678 NW2d 619 (2004). This Court will generally defer to an agency's interpretation of a statute the agency is delegated to administer, but this Court nevertheless reviews statutory language de novo and enforces plain and unambiguous language as written. *Vulic v Dep't of Treasury*, 321 Mich App 471, 477; 909 NW2d 487 (2017).

III. SALES AT RETAIL

The gravamen of NAB's refund request is that it should be allowed to defer owing use tax on *all* of its terminals because *some* of them would eventually be sold. NAB argues that *all*

of its terminals constitute "property purchased for resale," see MCL 205.94(c)(i), until such time as any particular terminal is removed from inventory for placement with a customer. We disagree.

NAB relies heavily on criticizing the Tax Tribunal's allegedly self-contradictory finding that NAB "does not engage in retail sales" despite recognizing that NAB does in fact sell some of its terminals at retail. In context, however, the Tax Tribunal found that despite making some sales of terminals, doing so was fundamentally not NAB's business. Rather, NAB's business was the provision of services. Such a finding is clearly "supported by competent, material, and substantial evidence on the whole record." *Catalina*, 470 Mich at 19. The evidence established that even though it was possible to purchase a terminal without a service agreement, there was essentially no reason why anyone *would* purchase a terminal without a service agreement, and the testimony strongly implied that NAB's witnesses had no idea whether such a standalone transaction had ever occurred. Indeed, NAB advertised itself as a provider of services and "free equipment," not as an equipment retailer. Therefore, the evidence is clear that although terminals were frequently sold outright, no such sales occurred without also entering into service agreements.[1]

The Tax Tribunal reasonably observed that, although NAB technically treated the terminals as separate transactions from the service agreements, as a *functional* matter, NAB's sold terminals were just as intertwined with its sales of services as NAB's placed-for-free terminals. The Tax Tribunal therefore invoked the "incidental to service" test, the function of which is "to determine whether the transaction is principally a transfer of tangible personal property or a provision of a service," which will in turn dictate whether sales tax or use tax applies. See *Catalina*, 470 Mich at 24-25. The Tax Tribunal accurately recited the criteria to consider:

> In determining whether the transfer of tangible property was incidental to the rendering of personal or professional services, a court should examine what the buyer sought as the object of the transaction, what the seller or service provider is in the business of doing, whether the goods were provided as a retail enterprise with a profit-making motive, whether the tangible goods were available for sale without the service, the extent to which intangible services have contributed to the value of the physical item that is transferred, and any other factors relevant to the particular transaction. [*Catalina*, 470 Mich at 26.]

The Tax Tribunal found that: (1) NAB's customers sought NAB's services as the object of their transactions; (2) NAB held itself out as a provider of services rather than a retailer of equipment; (3) NAB's business model was designed to profit from the sales of services; (4) NAB might sell terminals without services but did not do so in the normal course of its business; (5) the terminals were of minimal value compared to the services; and (6) petitioner had legitimate non-sales

[1] However, respondent exaggerates by claiming that the terminals were essentially worthless without a service agreement. The evidence established that once they were unlocked, they could be used with a different service provider.

reasons for maintaining separate documented transactions for the terminals and the services. All of those findings are "supported by competent, material, and substantial evidence on the whole record." *Catalina*, 470 Mich at 19. The Tax Tribunal therefore properly concluded that NAB's sales of terminals were merely incidental to its sales of services.

NAB criticizes the Tax Tribunal for "lumping together" its sold terminals with its placed-for-free terminals. We find this disingenuous, given NAB's attempt to defer use tax on *all* of its terminals due to the potential for selling *some* of the terminals. The evidence showed that NAB did not track its terminals separately, and it did not even document "sales" of the terminals separately from any other "revenue" generated from terminals (such as payment for damage). Respondent accurately points out that pursuant to MCL 205.52(3), which is part of the General Sales Tax Act, MCL 205.51 *et seq*.:

> Any person engaged in the business of making sales at retail who is at the same time engaged in some other kind of business, occupation, or profession not taxable under this act shall keep books to show separately the transactions used in determining the tax levied by this act. [. . .]

The Tax Tribunal noted that it lacked jurisdiction to consider what sales tax liability NAB might owe. Nevertheless, NAB's failure to maintain separate books or to treat the sold terminals in any distinguishable manner profoundly undermines its argument that respondent should treat the sold terminals in any distinguishable manner.

The Tax Tribunal properly concluded that NAB's terminals were not truly "purchased for resale," because only a minority were actually sold, because none of those sales were independent of NAB's services, *and* because all of the sales were merely incidental to NAB's services. These findings are "supported by competent, material, and substantial evidence on the whole record." *Catalina*, 470 Mich at 19. Respondent then correctly observes that under the Use Tax Act, merely "storing" property in Michigan is considered a taxable event. MCL 205.93(1); MCL 205.92(c). The Tax Tribunal correctly determined that NAB's terminals were all subject to the use tax upon NAB's purchase.

IV. DEPLOYMENT OUTSIDE MICHIGAN

NAB argues that the majority of its terminals are deployed outside of Michigan, and as a consequence they are not subject to the use tax. In *Brunswick Bowling & Billiards Corp v Dep't of Treasury*, 267 Mich App 682, 687; 706 NW2d 30 (2005), this Court stated: "The term 'use' as set out in [MCL 205.92(b)] does not encompass the withdrawal of inventory and subsequent distribution of such items in another state." Notably, *Brunswick* explicitly did not involve any question of whether the items at issue were subject to use tax based on their storage in Michigan. See *Brunswick*, 267 Mich App at 686 n 1. Respondent here *does* argue that NAB's terminals are subject to the use tax based on their storage in Michigan, rendering *Brunswick* entirely inapplicable. In any event, the issue in *Brunswick* was really whether an item could be considered withdrawn from the plaintiff's inventory merely because it was physically transported but never left the plaintiff's control and possession. *Brunswick*, 267 Mich App at 686-687.

Here, NAB's terminals left NAB's control and possession inside the state of Michigan, when it shipped the terminals. See *Sharper Image Corp v Dep't of Treasury*, 216 Mich App 698, 702; 550 NW2d 596 (1996) (explaining that the plaintiff transferred power over items when the items were delivered to the postal service). More importantly, *Brunswick* is premised on the assumption, unquestioned in that case, that the plaintiff's items were "inventory" of a kind otherwise exempt from the use tax. Because NAB did not "purchase the terminals for resale" within the meaning of the Use Tax Act, the terminals are *not* exempt from the use tax at the time of their purchase. *Brunswick* would only theoretically apply if NAB's storage of the terminals was not already a taxable event. Even then, *Brunswick* would only help NAB if NAB maintained possession and control over the terminals *until* the terminals left the state and *then* conveyed the terminals.

V. CONCLUSION

The Tax Tribunal properly found that NAB's terminals were subject to use tax at the time they are purchased by NAB. We therefore affirm. Respondent, being the prevailing party, may tax costs. MCR 7.219(A).

/s/ Brock A. Swartzle
/s/ Jane E. Markey
/s/ Amy Ronayne Krause