

STATE OF MICHIGAN  
COURT OF APPEALS

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VESTAX SECURITIES CORPORATION,

Plaintiff-Appellee,

v

DEPARTMENT OF TREASURY,

Defendant-Appellant.

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UNPUBLISHED

October 28, 2010

No. 292062

Court of Claims

LC No. 07-000065-MT

Before: O’CONNELL, P.J., and BANDSTRA and MARKEY, JJ.

PER CURIAM.

Defendant appeals by right from an order granting summary disposition to plaintiff pursuant to MCR 2.116(C)(10). This is a dispute involving the assessment of a tax under the Michigan Single Business Tax Act (SBT), MCL 208.1 to MCL 208.145.<sup>1</sup> Defendant argues that the Court of Claims erred in finding that plaintiff did not have a sufficient nexus with the state of Michigan to subject plaintiff to Michigan’s taxing jurisdiction. Because we agree, we reverse and remand for further proceedings.

Both a trial court’s determination of a motion for summary disposition and constitutional issues are reviewed de novo. *Fluor Enterprises, Inc v Dep’t of Treasury*, 477 Mich 170, 174; 730 NW2d 722 (2007). When reviewing a motion brought under MCR 2.116(C)(10), the court considers the affidavits, depositions, pleadings, admissions, and other evidence submitted by the parties in the light most favorable to the non-moving party. *Rose v Nat’l Auction Group, Inc*, 466 Mich 453, 461; 646 NW2d 455 (2002). Summary disposition is appropriate if there is no genuine issue regarding any material fact, and the moving party is entitled to judgment as a matter of law. *Id.*

Under the SBT, “every person with business activity in this state” was required to pay the single business tax. MCL 208.31(1). The SBT “encompasses taxation of services that are performed not only within the state . . . but also some that are performed out of state, as long as

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<sup>1</sup> The SBT was repealed by 2006 PA 325, and was replaced, effective December 31, 2007, with the Michigan Business Tax Act, 2007 PA 37, MCL 208.1101 *et seq.*

the reason those services are engaged in has its source within this state . . . .” *Fluor Enterprises*, 477 Mich at 175.

Under the Commerce Clause of the United States Constitution, a state has the power to compel a business to comply with its tax laws where, inter alia, the tax applies to an activity that has a substantial nexus with that state.<sup>2</sup> US Const, art I, § 8, cl 3; *Magnetek Controls, Inc v Dep’t of Treasury*, 221 Mich App 400, 406; 562 NW2d 219 (1997). The burden is always on the state to establish the necessary facts to sustain a claim for taxes. *Gillette Co v Dep’t of Treasury*, 198 Mich App 303, 318; 497 NW2d 595 (1993). In *Magnetek*, the Court cited the following standard, derived from *Quill Corp v North Dakota*, 504 US 298, 315; 112 S Ct 1904; 119 L Ed 2d 91 (1992), to satisfy the substantial nexus requirement:

While a physical presence . . . is required, it need not be substantial. Rather, it must be demonstrably more than a “slightest presence.” . . . And it may be manifested by the presence in the taxing State of . . . property or the conduct of economic activities in the taxing State performed by the vendor’s personnel or on its behalf. [*Magnetek Controls*, 221 Mich App at 411, quoting *In re Orvis Co, Inc v Tax Appeals Tribunal of the State of New York*, 86 NY2d 165, 178; 630 NYS2d 680; 654 NE2d 954 (1995).]

The Court upheld the Court of Claims’ determination that Magnetek’s out-of-state sales were not subject to the SBT under MCL 208.42 because there existed a substantial nexus required by the Commerce Clause for the other states to impose a tax on that activity. *Magnetek Controls*, 221 Mich App at 412. Specifically, Magnetek’s employees were present in the other states for two weeks a year of solid sales effort, and independent sales representatives were permanently present selling plaintiff’s lines along with those of other companies. *Id.* at 402-405.

Here, defendant asserts that plaintiff had agents in the state acting on its behalf to solicit requests for securities transactions. Plaintiff explained in affidavits that its business in Michigan consisted of contractual relationships with independent registered representatives (IRRs) that used plaintiff to facilitate securities transactions. IRRs could only access a national securities exchange through association with a securities broker-dealer, such as plaintiff. The customers of an IRR would request a securities transaction from the IRR, and the IRR in turn would rely on defendant to make the transaction. Plaintiff contracted with Pershing, LLC, to process and administer securities transactions on stock exchanges. Plaintiff had no ownership interest in Pershing. The IRRs ran their own offices and offered services in addition to securities transactions.

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<sup>2</sup> In this case, the “substantial nexus” requirement is the only factor at issue. However, there is a four-part test to determine if a state tax complies with the Commerce Clause. Courts will sustain a tax under the Commerce Clause as long as it: (1) is applied to an activity which has a substantial nexus with the taxing state, (2) is fairly apportioned, (3) does not discriminate against interstate commerce, and (4) is fairly related to services provided by the taxing state. *Guardian Indus Corp v Dep’t of Treasury*, 198 Mich App 363, 376; 499 NW2d 349 (1993).

In finding no substantial nexus in this case, the lower court cited the reasoning in *Scholastic Book Clubs, Inc v Dep't of Treasury*, 223 Mich App 576, 580; 567 NW2d 692 (1997). There, school teachers facilitated the sale of books to schoolchildren. The Court recited established law holding that “an out-of-state vendor whose only contacts with the taxing state are by mail or common carrier, or whose business activity is limited to the mere solicitation of sales, lacks the substantial nexus required by the Commerce Clause.” In concluding that there was no substantial nexus, the Court stated:

Michigan teachers who receive plaintiff’s catalogs are clearly not its employees. Under Michigan law, they are also not plaintiff’s agents. There is no indication that Michigan teachers have the authority to bind plaintiff. Further, plaintiff has no control over the teachers; the teachers are under no obligation to participate in plaintiff’s program. [*Id.* at 583-584.]

Rejecting the state’s argument that the teachers constituted a sales force on behalf of Scholastic Book Clubs, Inc., the Court held “that the use of teachers, without more, does not establish a substantial nexus with, or physical presence in, this state.” *Id.* at 582.

Unlike *Scholastic Book Clubs*, the instant case involves a contractual relationship between plaintiff and the IRR that is specific to the IRR’s utilization of plaintiff’s services. Moreover, the IRRs were required to use a broker-dealer, such as plaintiff, to conduct their customers’ transactions. The contractual relationship between plaintiff and the IRRs was more formal, direct, and specific than the *Scholastic Book Clubs*’ arrangement. Additionally, the IRRs were plaintiff’s agents. Before its repeal in 2009, the Uniform Securities Act defined an agent, in part, as “any individual other than a broker-dealer who represents a broker-dealer or issuer in effecting or attempting to effect purchases or sales of securities.” MCL 451.801(c);<sup>3</sup> see also *Vestax Securities Corp v McWood*, 280 F 3d 1078, 1080, 1082 (CA 6, 2002)(holding investor-customers of plaintiff’s registered agents or representatives could arbitrate claims against the plaintiff despite the investors having little contractual or transactional relationship with the plaintiff because the agents or representatives were “associated person[s]” under a National Association of Securities Dealers rule).

But in evaluating whether there was a substantial nexus between Michigan and plaintiff’s business activities sufficient to tax, the relevant question is not premised on the definition of the legal relationship between plaintiff and the IRR under securities law or the label used to characterize the relationship. Rather, under the Commerce Clause, the question is whether a substantial nexus was established by the physical presence in the state of a person doing business on plaintiff’s behalf. We conclude that the contractual relationship between IRRs and plaintiff resulted in such a presence. The IRRs certainly created business for plaintiff originating in the state because the IRRs were required to use a securities broker-dealer, such as plaintiff, in order to process the orders of the IRRs’ customers. And, as in *Magnetek Controls*, 221 Mich App at 409, 412, the activity of independent sales representatives permanently located in the state

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<sup>3</sup> The Uniform Securities Act, including MCL 451.801, was repealed as of October 1, 2009. MCL 451.2702.

resulting in sales for plaintiff is “conduct of economic activities in the taxing State performed by the vendor’s personnel or on its behalf.” Even though the IRRs ran their own independent businesses, plaintiff used the term “independent registered *representatives*” to indicate that the IRRs were its representative in the state and used the IRRs pursuant to the contracts to generate orders to conduct securities transactions. The IRRs were acting on their own behalf and on behalf of the broker-dealer they chose pursuant to contract to receive a commission for executing the securities transactions.<sup>4</sup> This activity satisfies the constitutional substantial nexus requirement.

Defendant also argues that a penalty for not filing tax returns was properly assessed on plaintiff. We decline to address this issue because whether a penalty is appropriate should first be addressed by the lower court with the benefit of a fully developed record.

We reverse and remand for further proceedings consistent with this opinion. We do not retain jurisdiction. No taxable costs pursuant to MCR 7.219, a question of public policy involved.

/s/ Peter D. O’Connell  
/s/ Richard A. Bandstra  
/s/ Jane E. Markey

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<sup>4</sup> We note that plaintiff contends that it works for the IRR’s. Even if we accept that view of the facts here, the relationship is symbiotic, with the IRR’s also providing a benefit to plaintiff and thus providing the necessary business nexus with Michigan.