

STATE OF MICHIGAN
COURT OF APPEALS

SIDNEY FRANK IMPORTING COMPANY,
INC.,

UNPUBLISHED
December 4, 2012

Petitioner-Appellant,

v

No. 306742
Tax Tribunal
LC No. 00-383623

DEPARTMENT OF TREASURY,

Respondent-Appellee.

Before: BORRELLO, P.J., and FITZGERALD and OWENS, JJ.

PER CURIAM.

Petitioner appeals by right from a Michigan Tax Tribunal (MTT) opinion and order that granted summary disposition in favor of respondent. On appeal, petitioner argues that the MTT erred in finding that: (1) the transaction at issue was not a “sale” under MCL 208.7(1)(a); (2) petitioner waived its right to relief under MCL 208.69; (3) petitioner was not entitled to relief under MCL 208.69, and; (4) the application of Michigan tax law to petitioner in this case was not unconstitutional. We affirm in part, reverse in part, and remand.

I. BASIC FACTS AND PROCEDURAL HISTORY

Petitioner initiated the proceedings in this case by filing a petition in the MTT on February 23, 2010. Respondent filed a response in opposition. The parties stipulated to the following facts which were adopted by the tribunal:

1. Petitioner is a New York corporation whose principal office is located at 20 Cedar Street, Suite 203, New Rochelle, New York 10801.
2. Respondent, Michigan Department of Treasury (the “Respondent”), is a department of the State of Michigan, and is the governmental authority responsible for administering the Single Business Tax (“SBT”) Act, MCL § 208.1 et. seq., now repealed, and the taxes that were applicable for the year at issue which are the subject of this Petition.
3. Petitioner’s federal employer identification number is XX-XXX7884.

4. Petitioner is classified as an S Corporation for federal and state income tax purposes.
5. Petitioner filed its 2004 SBT return.
6. Petitioner also filed an amended 2004 SBT return on or about October 16, 2007. The tax return was amended to reflect an adjustment by the Internal Revenue Service to Petitioner's 2004 federal income tax return, which adjustments were unrelated to the Grey Goose transaction and the issues involved in this controversy.
7. Petitioner's initial and amended 2004 SBT returns reflected the gain on the sale of Petitioner's assets related to the Grey Goose vodka product line, as described in more detail below.
8. Respondent audited Petitioner's 2004 SBT return, utilizing Petitioner's amended return as a basis for the audit (the amended return is hereinafter referred to as the "Tax Return").
9. Petitioner disagreed with Respondent's Audit Determination.
10. Respondent issued its Bill for Taxes Due ("Intent to Assess") number R498688 on or about November 10, 2009.
11. Following receipt of the Intent to Assess, on or about November 20, 2009, Petitioner sent checks to Respondent for the purpose of paying the taxes and interest reflected in the Intent for all years other than the 2004 tax year.
12. Respondent issued its Final Bill for Taxes Due ("Final Assessment") Number R498688 (the "Assessment") on or about January 19, 2010. Although Petitioner previously sent the checks, the Assessment continued to reflect taxes and interest for 2005, 2006 and 2007. Petitioner and Respondent are continuing their efforts to resolve the payment issue for 2005-2007 and will supplement this Stipulation when the issue is resolved.
13. Petitioner appealed the Assessment upon the commencement of this action by the filing of its Petition on February 23, 2010.
14. Petitioner is an importer and distributor of wines and spirits. Petitioner's business activity in Michigan is limited solely to sales of wine and spirits—primarily to the Michigan Liquor Control Commission.
15. Petitioner maintains no business locations within the State. Petitioner does maintain inventory stock at its Michigan broker's location in Highland Park, Michigan.

16. In addition to its business activities of importing and distributing liquors, Petitioner also owned trade names or licenses to produce and sell several of the brands it sold, including Grey Goose vodka.
17. Prior to 2004, Petitioner owned the exclusive rights to trademark and license a product line known as Grey Goose vodka.
18. Unlike other products imported and distributed by Petitioner that were produced by unrelated third-party producers, Grey Goose vodka was produced by Petitioner's affiliate, Grey Goose SAS ("SAS"). SAS was a French company that produced, shipped, and owned the manufacturing plant for Grey Goose vodka.
19. Petitioner's ownership of SAS was through an intermediate holding company known as Grey Goose Bottling Co., LLC ("GGB"), a Delaware limited liability holding company that owned 100% of SAS.
20. SAS produced Grey Goose vodka in France and shipped it to Petitioner, its sole customer in the United States.
21. Petitioner sold Grey Goose vodka products to its customers, liquor and beverage distributors within Michigan and elsewhere in the United States.
22. Petitioner's involvement with the Grey Goose line of business was completely different and functionally unique from all of Petitioner's other business activities.
23. Grey Goose represented the first and only product line developed and manufactured by Petitioner, and the only aspect of its activities that was handled through the use of separate companies and entities.
24. In 2004, pursuant to an Asset Purchase Agreement among Petitioner, SAS and the purchaser, Bacardi, Limited, Petitioner sold all of its tangible and intangible assets relating to the Grey Goose vodka product line, including inventory and all intellectual property rights relating to the production, distribution, and marketing of the Grey Goose vodka. (The "Grey Goose Transaction.")
25. In 2004, as part of the same transaction, Petitioner's affiliate, SAS, also sold its respective assets to the purchaser, Bacardi, Limited.
26. The adjusted purchase price paid by purchaser to the selling entities was \$2,278,588,589. Of this amount, \$2,144,993,971 was paid to Petitioner and allocated by Petitioner and the purchaser as follows:

Finished inventory in France	\$12,010,430
Dry goods – gin	\$658,579
Prepaid – media	\$3,127,589
Prepaid – sponsorships	\$461,000
Inventory in USA	\$9,110,778
Intangible and intellectual property	\$2,119,625,596
Total	\$2,144,993,971

27. The Grey Goose Transaction was the largest financial transaction in the Petitioner's history.
28. Upon information and belief, the Grey Goose Transaction was one of the largest transactions in the history of the liquor industry.
29. Petitioner recognized a substantial gain from the transaction, which gain was included in Petitioner's federal income tax return as taxable income, and consequently included by Petitioner in its tax base for its 2004 Tax Return.
30. In addition to including more than \$2 billion of gain in its SBT tax base for the 2004 tax year, Petitioner reflected the sale from the transaction in the denominator of the sales factor portion of the apportionment formula used to apportion Petitioner's tax base among Michigan and other states in which Petitioner was taxable.
31. For federal income tax purposes, the gain reflected on Petitioner's federal income tax return, Form 1120S, was allocated to its shareholders in accordance with their percentage ownership interests in Petitioner.
32. Petitioner's shareholders also reflected the gain in their 2004 federal and resident state individual income tax returns on an unapportioned basis.
33. To the extent that Petitioner had nexus with various states that imposed an individual income tax, Petitioner's shareholders reflected the gain in their 2004 nonresident state individual income tax returns for the entire gain allocated to each shareholder, which was then allocated or apportioned to each state in accordance with that state's allocation or apportionment rules. The shareholders filed such returns in approximately 35 states.

Petitioner agrees to provide summaries of such returns, or copies of the returns, if available, upon the request of Respondent or the Tribunal.

34. In its 2004 SBT return, Petitioner reported total sales in Michigan (sales of products distributed by it) of \$18,754,142 over total sales everywhere of \$2,542,422,073.
35. With respect to the 2004 calendar year, Respondent recalculated the denominator of the sales factor by removing the proceeds of the Grey Goose sale.
36. Specifically, Respondent removed \$2,176,474,888 from the denominator of sales factor, recalculating the total Michigan sales of \$18,754,142 over a 2004 sales denominator of \$365,947,185, which increased the 2004 Michigan sales factor apportionment percentage from 0.7376% to 5.1248%, and the overall Michigan apportionment percentage from 0.8891% to 4.8376%.
37. Respondent's audit adjustment, as reflected in the Assessment, ultimately increased Petitioner's Michigan tax base by \$50,228,911, to \$61,539,162, and resulted in an asserted tax increase of \$858,914, plus additional interest.
38. If Petitioner prevails on the legal issues relating to the determination of the sales factor of the apportionment formula, the Assessment should be cancelled in full.
39. Paragraphs 11 and 12 of the Stipulated Facts are hereby modified to reflect that the payments made by Petitioner for the 2005-2007 years have been accepted by Respondent and discharge all outstanding liability for those years. Respondent has issued a corrected Final Assessment, which reflects only the amount assessed for 2004 with respect to the Grey Goose transaction and apportionment issues.

Petitioner filed a motion for summary disposition pursuant to MCR 2.116(C)(10). Respondent filed a brief in opposition and filed a motion for summary disposition pursuant to MCR 2.116(C)(10) and MCR 2.116(I)(2). The tribunal issued a written opinion and order that denied petitioner's motion, granted respondent's motion for summary disposition pursuant to MCR 2.116(C)(10), and affirmed Assessment No. R498688. Petitioner now appeals.

II. STANDARD OF REVIEW

An MTT grant of summary disposition pursuant to MCR 2.116(C)(10) is subject to review de novo. *Paris Meadows, LLC v City of Kentwood*, 287 Mich App 136, 141; 783 NW2d 133 (2010). The proper interpretation and application of statutory language is a question of law also subject to review de novo. *Id.*

III. THE GREY GOOSE TRANSACTION

The SBTA, now repealed,¹ was a modified value-added tax that imposed a specific tax on the adjusted tax base of every person with business activity in Michigan after that activity was allocated or apportioned to Michigan. MCL 208.31(1); *ANR Pipeline Co v Dep't of Treasury*, 266 Mich App 190, 198-199; 699 NW2d 707 (2005). The SBTA defined “business activity” as follows:

“Business activity” means a transfer of legal or equitable title to or rental of property, whether real, personal, or mixed, tangible or intangible, or the performance of services, or a combination thereof, 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, but shall not include the services rendered by an employee to his employer, services as a director of a corporation, or a casual transaction. Although an activity of a taxpayer may be incidental to another or other of his business activities, each activity shall be considered to be business engaged in within the meaning of this act. [MCL 208.3(2).]

The applicable tax base was defined as “business income, before apportionment or allocation.” MCL 208.9(1). Business income for an S corporation, such as petitioner, was defined as federal taxable income as defined by section 63 of the internal revenue code. MCL 208.3(3); MCL 208.5(3). Taxpayers that conducted business both inside and outside of Michigan were taxed based on the portion of their business activity apportioned to Michigan by means of formulas provided in the SBTA. MCL 208.41. The apportionment was calculated by multiplying petitioner’s tax base by a percentage, calculated as the sum of the percentages of the property factor, payroll factor, and sales factor. MCL 208.45. These three factors are fractions, calculated as the portion of property, payroll, or sales within Michigan, divided by the total property, payroll, or sales of the taxpayer worldwide. MCL 208.46; MCL 208.49; MCL 208.51. “The sales factor is a fraction, the numerator of which is the total sales of the taxpayer in this state during the tax year, and the denominator of which is the total sales of the taxpayer everywhere during the tax year.” MCL 208.51(1). For the year 2004, the SBTA provided 90% weighting to the sales factor, with 5% weighting applied to both the property and payroll factor. MCL 208.45a(1).²

¹ The SBTA was repealed by 2006 PA 325.

² MCL 208.45a(1) provides:

(1) Except as provided in subsection (4) and for tax years beginning after December 31, 1998 and before January 1, 2006, all of the tax base, other than the tax base derived principally from transportation, financial, or insurance carrier

Petitioner argues that the amount received in the Grey Goose transaction should be included in the sales factor denominator. Respondent disagrees. As a result, petitioner's proposed sales factor is 0.8891% and respondent's 4.8376%. Therefore, the issue in this case is whether the Grey Goose transaction constituted a "sale" and was thus required to be included in the denominator of the sales factor.

The SBTA defined "sale" as follows:

(a) "Sale" or "sales" means the amounts received by the taxpayer as consideration from the following:

(i) The transfer of title to, or possession of, property that is stock in trade or other property of a kind which would properly be included in the inventory of the taxpayer if on hand at the close of the tax period or property held by the taxpayer primarily for sale to customers in the ordinary course of its trade or business.

(ii) The performance of services, which constitute business activities other than those included in subparagraph (i), or from any combination of business activities described in this subparagraph and subparagraph (i).

(iii) The rental, lease, licensing, or use of tangible or intangible property which constitutes business activity. [MCL 208.7(1)(a)(i)-(iii).]

Petitioner argues only that the transaction constituted a sale under MCL 208.7(1)(a)(iii) as a "use of intangible property which constitutes business activity." Respondent argues that MCL 208.7(1)(a)(iii) applies only to "transactions where the taxpayer allows a person to possess and use the property, and not sales that transfer title and possession of the property."

Petitioner's argument fails. "Sales" clearly fit within the category of "business activity" as defined by the SBTA. However, as respondent argues, they are not equivalent. If this Court were to adopt petitioner's interpretation of MCL 208.7(1)(a)(iii), virtually any "business activity" would constitute a "sale." If the Legislature had intended the terms to be synonymous, it would have had no need to provide separate definitions. MCL 208.7(1)(a) defines "sale" as the consideration received by a taxpayer for sale of property that is "stock in trade" or inventory, the rendering of services, or the rental lease, licensing or use of property. Petitioner's sale of the Grey Goose brand fits none of these definitions. The amount received by petitioner in the Grey Goose transaction was not for the "use" of the Grey Goose brand name; rather, it was for the

services or specifically allocated, shall be apportioned to this state by multiplying the tax base by a percentage, which is the sum of all of the following percentages:

- (a) The property factor multiplied by 5%.
- (b) The payroll factor multiplied by 5%.
- (c) The sales factor multiplied by 90%.

transfer of title to the Grey Goose brand as a whole. Petitioner was not temporarily renting, leasing, licensing or permitting another to use the Grey Goose name—petitioner sold the entire brand.

Further, the doctrine of ejusdem generis supports the conclusion that “use” is properly interpreted in the context of rental or lease transactions. As our Supreme Court has stated:

“[Ejusdem generis] is a rule whereby in a statute in which general words follow a designation of particular subjects, the meaning of the general words will ordinarily be presumed to be and construed as restricted by the particular designation and as including only things of the same kind, class, character or nature as those specifically enumerated.” [*Sands Appliance Servs, Inc v Wilson*, 463 Mich 231, 242; 615 NW2d 241 (2000), quoting *People v Brown*, 406 Mich 215, 221; 277 NW2d 155 (1979), quoting 73 Am Jur 2d, Statutes, § 214, pp 407-408 (alteration by *Sands*).]

Thus, “use” should be understood as falling within a category that includes renting, leasing, and licensing. Each of these involves the exchange of consideration for the right to use, possess, and/or occupy tangible or intangible property for some term. There is no passing of title; that is addressed in MCL 208.7(1)(a)(i), but only with respect to “property that is stock in trade or other property of a kind which would properly be included in the inventory of the taxpayer if on hand at the close of the tax period or property held by the taxpayer primarily for sale to customers in the ordinary course of its trade or business.”

Under petitioner’s interpretation of “use,” almost any activity would fit the definition. As a result, anything that qualified as “business activity” under the SBTA could be “used” and thus constitute a “sale.” This reading would render the definition of “sale” nugatory, as merely an equivalent of “business activity.” This strained interpretation of “sale” would result in impractical and unintended application of the SBTA. Thus, the tribunal did not err in ruling that the Grey Goose was transaction was not a “sale” within the meaning of MCL 208.7(1).

IV. RELIEF UNDER MCL 208.69

Petitioner argues that it was entitled to an alternate method of apportionment under MCL 208.69. MCL 208.69 provides an option for a taxpayer to petition for alternative apportionment “[i]f the apportionment provisions of [the SBTA] do not fairly represent the extent of the taxpayer’s business activity in this state.” MCL 208.69(1). MCL 208.69 explicitly provides that any “alternate method [of apportionment] will be effective only if it is approved by the commissioner.” The MTT concluded that petitioner had waived this issue because it failed to petition the commissioner for alternative apportionment.

However, on appeal petitioner argues, and respondent concedes, that it filed such a petition with the commissioner of revenue within the meaning of MCL 208.69. The parties agree that petitioner raised alternative apportionment issues in a manner sufficient to comply with MCL 208.69 through correspondence that petitioner’s attorney Timothy Noonan had with John McAndrew, a senior auditor with the Michigan Department of Treasury. This correspondence was not admitted into the record in the MTT; however, on July 12, 2012 this

Court granted petitioner's motion to supplement the record. Petitioner then filed a revised reply brief and attached a copy of a letter from Noonan to McAndrew dated July 10, 2009. The letter confirms that a request for alternative apportionment was made. Petitioner also attached Noonan's reply to McAndrew, which stated, "I acknowledge receipt of your letter dated 7/10/09, which I am forwarding to my Supervisors in Lansing for review. I will advise you of their response as soon as received." The parties agree that petitioner never received a response to its request.

Because the parties did not present this evidence to the MTT, the MTT concluded that petitioner had waived the issue and never reached the merits of the argument. However, now that this Court has allowed petitioner to supplement the record, it is clear that petitioner did not waive this matter. Therefore, we remand this issue to the MTT for consideration of the newly supplied documents and for a determination of whether petitioner was entitled to alternative apportionment under MCL 208.69.

V. THE APPORTIONMENT CALCULATION

Petitioner argues that respondent's calculation of the sales factor has "led to a grossly distorted result" that is "out of all appropriate proportions," and is unconstitutional.

Petitioner's arguments are conclusory and without merit. Petitioner fails to meet the applicable burden of providing clear and cogent evidence of such a distorted result. Petitioner cannot contend that the Grey Goose transaction was attributable solely to activities occurring outside of Michigan. Petitioner sold the Grey Goose brand for over \$2 billion dollars because it was and is a popular and high-selling brand of vodka. Petitioner sold this brand in Michigan, and those sales contributed to the value of the brand. As such, respondent is entitled to tax a portion of the proceeds of the transaction as provided in the SBTA. Further, arguing that the Grey Goose transaction is attributable only to non-Michigan activities constitutes "geographical accounting," an argument that does not pass constitutional muster. See *Corning*, 212 Mich App at 8. In any event, state taxation is not unconstitutional merely because it *might* tax some activity that occurred outside the taxing state; such variances are recognized and accepted in this area of jurisprudence. Petitioner's arguments surrounding this single transaction, no matter how strong, do not render the apportionment unconstitutional. As this Court has stated, "single-element analysis does not suffice regardless of the strength of the arguments that might be thereby advanced." *Id.* at 7. Thus, the tribunal did not err in rejecting petitioner's constitutional challenge to respondent's apportionment calculation in this case.

Affirmed in part, reversed in part, and remanded for proceedings consistent with this opinion. We do not retain jurisdiction. No costs are taxable pursuant to MCR 7.219, neither party having prevailed in full.

/s/ Stephen L. Borrello
/s/ E. Thomas Fitzgerald
/s/ Donald S. Owens