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What Part Of "In Michigan" Do You Not Understand? Michigan Court Of Appeals Rejects Attempt To Impose Use Tax On Bowling Balls Used Outside Of Michigan

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The Michigan Court of Appeals recently rejected an attempt to impose the state's use tax on items shipped outside of Michigan for use outside of Michigan.[1] The lesson to be drawn is that what might be subject to use tax in one state might *not* be subject to use tax in another state due to different interpretations of the law. Taxpayers need to examine the laws of each state in particular.

The Promotional Use Of A Manufacturer's Product

Brunswick is a Delaware corporation headquartered in Michigan. Brunswick's business includes manufacturing and selling bowling balls at retail. Brunswick also sponsors bowling tournaments in Michigan and elsewhere for the Professional Bowlers Association. Brunswick shipped bowling balls from Michigan to bowling tournaments taking place outside of Michigan, for possible use as promotional gifts to bowlers. A Brunswick representative located at the tournament site received the bowling balls and stored them on shelf space at the bowling lanes. When necessary, the representative removed a ball from storage, drilled it, and gave it to a Brunswick-sponsored professional bowler for use at the tournament. Bowling balls that were not given away were returned to Brunswick's facilities in Michigan. Thus, at the time the balls were removed from Brunswick's facility in Michigan, the company was uncertain as to whether the balls would be given away for promotion purposes or returned to inventory.

Were The Bowling Balls Used In Michigan

Michigan use tax is imposed on the "the privilege of using, storing, or consuming tangible personal property in this state . . . ."[2] "Use" means "the exercise of a right or power over tangible personal property incident to the ownership of that property including transfer of the property in a transaction where possession is given."[3]

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[1] *Brunswick Bowling & Billiards Corp. v. Dep't of Treasury*, ___ N.W.2d ___, 2005 WL 1992370 (Mich. Ct. App. Aug. 18, 2005).

[2] Mich. Comp. Laws § 205.93(1).

[3] Mich. Comp. Laws § 205.92(b).

The Michigan Department of Treasury ("Department") assessed use tax on the bowling balls shipped outside of Michigan. The Department maintained that Brunswick's withdrawal of the bowling balls from inventory in Michigan constitutes a taxable "use." Brunswick responded that the bowling balls were not withdrawn from inventory until they were given away at the tournaments, and, since that transfer occurred in-person and outside of Michigan, use tax did not apply.

"Use" Must Be In Michigan

The Court agreed with Brunswick. The Court noted that "[t]he question . . . is whether plaintiff's shipment of items elsewhere constitutes a 'use' in Michigan." *Brunswick*, slip. op. at 2. The Court said that "[u]nder the plain meaning of the statute, in order to be taxed under the [use tax act], a taxpayer must perform in Michigan one of the activities listed in the definition of 'use.'" *Id.* at 3. The Court held that "[t]he term 'use' as set out in the statute does not encompass the withdrawal of inventory and subsequent distribution of such items in another state. Because the items in dispute remained in plaintiff's control and possession when they were sent to other states for *potential* promotional or giveaway purposes, their 'use' for these purposes did not occur in Michigan." *Id.* (emphasis added).

The Department attempted to justify its position by relying on a prior administrative hearing[4] in the Department's favor and on a "tax training" document supporting the Department, urging judicial deference to that interpretation. The administrative hearing involved Wilson Sporting Goods. Wilson manufactured golf balls at a plant in Michigan and donated the balls to golf professionals for use in tournaments outside of Michigan. Relying on the phrase "consuming tangible personal property in this state" in the Michigan use tax imposition statute, the Michigan Board of Tax Appeals held that the "removal from inventory constitutes an act within the category of 'otherwise consuming.'" Thus, the Board ruled that "as 'users' or persons 'otherwise consuming' golf balls within the State of Michigan, Appellants are liable for payment of Use Tax." In reaction to the administrative hearing, the Court held that "[i]t is questionable whether that case is factually on point and addresses the legal question raised here" and in any event, "an administrative interpretation is not conclusive and cannot be used to overcome a logical reading of the statute." *Brunswick*, slip. op. at 4.

With respect to the administrative "tax training" document (which basically echoed the Board's conclusion in the hearing), the Court held that, "[i]n order for an agency regulation, statement, standard, policy, ruling, or instruction of general applicability to have the force of law, it must fall under the definition of a properly promulgated rule. If it does not, it is merely explanatory. . . . While the 'tax training' document may be used as a guide, it was not promulgated as an administrative rule, and therefore does not have the force of law." *Id.*

[4] *See Wilson Sporting Goods Co. v. Dep't of Treasury*, No. 1297 (Mich. B.T.A. 1977).

Implications

The *Brunswick* case appears to be an aberration resulting from the rather unique facts in the case and the Michigan Court of Appeal's reading of the Michigan use tax statute. The Michigan Court appears to have placed considerable emphasis on Brunswick's argument that, if the promotional items are not given away in another state, they are returned to Brunswick's Michigan inventory and therefore, no "use" occurred in Michigan. As the Michigan Court apparently concluded, activities outside of Michigan should not result in use tax being owed to Michigan. The decision does not indicate whether Brunswick paid use tax in the states in which the bowling balls were given away.

State-By-State Differences

It is unclear whether other state courts would draw such fine lines if faced with similar facts. For example, the Ohio Supreme Court reached just the opposite conclusion in a similar use tax case, which, by happenstance, also relates to bowling. In *Women's International Bowling Congress, Inc. v. Porterfield*, 25 Ohio St. 2d 271, 267 N.E.2d 781 (1971), the Ohio Supreme Court considered whether an Ohio-based organization that operated a bowling awards program "used" the emblems and awards that were shipped from its headquarters in Ohio to bowling leagues and other recipients located outside the state. In many cases, the taxpayer simply stored the emblems it received from its supplier in the unopened envelopes before forwarding them on to recipients outside the state. In other circumstances, however, the taxpayer's employees opened the original bulk packages, selected certain emblems and then re-packed commingled items for shipment. Finally, employees also removed certain awards from their individual wrappings for special engraving work or for proper sizing before being mailed to the bowling leagues on some occasions.

Based on these facts, the Ohio Supreme Court concluded that the taxpayer "used" the emblems and awards in Ohio. Like the Michigan statute, Ohio defines "use" as "the exercise of any right or power incidental to the ownership of the thing used."[5] Since the taxpayer made decisions regarding the distribution of the emblems from its Ohio location, selected and re-packaged items prior to shipment, and in some cases even engraved the items, the Court rejected the taxpayer's argument that such items were not "used" in Ohio, but were merely stored for use outside the state.

Reconcilable Differences?

Although Ohio's statutory definition of "use" is functionally identical to Michigan's, the Ohio Supreme Court interpreted it differently from the Michigan Court in *Brunswick*. This might be explained by the factual differences in each case. For instance, unlike the Ohio case, the taxable "use" asserted by the Department in *Brunswick* was the withdrawal of

[5] *See* Ohio R.C. 5741.01(C). The current Ohio statute adds a new sentence to specifically apply to the distribution of promotional items to Ohio residents. In its current form, Ohio R.C. 5741.01(C) further states that "[a] thing is also "used" in this state if its consumer gives or otherwise distributes it, without charge, to recipients in this state."

the bowling balls from inventory in Michigan. Clearly, the taxpayer in the Ohio case did more than merely withdraw the taxed items from inventory -- it performed other assembly and engraving activities in some cases. And unlike the facts in *Brunswick*, the awards and emblems were never under the taxpayer's control and possession once they left Ohio.

Application of *Women's International Bowling Congress* in subsequent Ohio decisions suggests, however, that the differing outcomes result from more than factual distinctions between the cases. On other occasions, the Ohio Supreme Court has expressly held that removing items from inventory constitutes a taxable "use" in Ohio. *See, e.g.*, *International Thomson Publishing, Inc. v. South-Western Publishing Co.,* 79 Ohio St. 3d 415 (1997)(textbook seller "used" textbooks by removing them from inventory and sending them free-of-charge to teachers for promotional purposes); *Norandex, Inc. v. Limbach*, 69 Ohio St. 3d 26, 30 (1994)(sample cases "used" in Ohio because the taxpayer "decided the sequence in which [branch offices] would receive the cases, removed the cases from the pallets to place on trucks, and directed a carrier to deliver the cases" outside the state). Thus, Ohio has consistently held that the type of activities at issue in *Brunswick* are subject to tax in Ohio.

Conclusion

In short, every state has different rules in this area. Statutory definitions of "use" may differ among states. Even in those states with similar definitions, each state's interpretations may vary. For this reason, it is very important to look at these issues on a state-by-state basis.■

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