

STATE OF MICHIGAN
DEPARTMENT OF ENERGY, LABOR & ECONOMIC GROWTH
MICHIGAN TAX TRIBUNAL

Kelly Properties, Inc. and Kelly Services, Inc.,
Petitioners,

MTT Docket Nos. 319360 and 319361

v

Michigan Department of Treasury,
Respondent.

Tribunal Judge Presiding
Rachel J. Asbury

FINAL OPINION AND JUDGMENT

ORDER CONSOLIDATING MTT DOCKET NOS. 319360 AND 319361

ORDER GRANTING PETITIONERS' MOTION FOR SUMMARY DISPOSITION

ORDER DENYING RESPONDENT'S MOTION FOR SUMMARY DISPOSITION

INTRODUCTION

Petitioner Kelly Services (“Kelly Services”) is a Delaware corporation with headquarters located in Troy, Michigan. Petitioner timely filed single business tax returns for the 1997 through 2000 tax years. Respondent audited Kelly Services for that period and issued Final Assessment L743510 on June 9, 2005, for single business tax in the amount of \$260,675 plus interest. There is no controversy over Petitioners’ exclusion of the royalty income received from its foreign subsidiaries from the calculation of the sales factor for apportionment purposes under MCL 208.51 and from the calculation of gross receipts under ML 208.7(3), for the tax years at issue. The Final Assessment was based on the inclusion of royalty income, in the calculation of Petitioner’s sales factor under MCL 208.51 and in the calculation of gross receipts under MCL 208.7(3).

Petitioner Kelly Properties (“Kelly Properties”) is a Michigan corporation with headquarters located in Troy, Michigan. Petitioner timely filed single business tax returns for the 1997 through 2000 tax years. Respondent audited Kelly Properties for that period and issued Final Assessment L755152 June 9, 2005, for single business tax in the amount of \$49,727 plus interest for the 1997 tax year.

Petitioners requested informal conferences in both matters, which were held jointly on March 4, 2005. The Hearing Referee rejected Respondent’s position and cancelled the assessments against both Petitioners. On May 27, 2005, Daniel Greenberg, Administrator of Respondent’s Office of Hearings, issued a Decision and Order, in which he failed to adopt the Hearing Referee’s recommendations and upheld the assessments against both Petitioners. Petitioners timely filed petitions with the Tribunal appealing Respondent’s Decisions and Orders on July 13, 2005.

On May 25, 2007, Petitioners filed Motions for Summary Disposition under MCR 2.116(C)(10) and requested the Tribunal to cancel and set aside Respondent’s Decisions and Order of Determination upholding the Intents to Assess. On June 15, 2007, Respondent filed an Answer and Brief in Opposition to Petitioners’ Motion for Summary Disposition and requested that the Tribunal grant Summary Disposition in its favor. On July 2, 2007, Petitioners filed a response to Respondent’s Answer and Brief in Opposition to Petitioners’ Motion for Summary Disposition.

On July 16, 2007, the Tribunal held oral arguments on Petitioners’ and Respondent’s Motions for Summary Disposition.

BACKGROUND

Petitioners, Kelly Services and Kelly Properties, are affiliated companies. Petitioner Kelly Services is in the business of providing temporary staffing services. Kelly Properties manages assets used in the business operations of Kelly Services and other affiliated companies. Kelly Properties owns the real estate and manages the buildings, investments, trademarks, and trade names on behalf of the affiliated companies. The trademarks and trade names are used solely within the network of Kelly Properties' affiliated companies. Kelly Properties licenses the use of the trademarks and trade names to Kelly Services and Kelly Services has the right to sublicense the trademarks and trade names to its foreign affiliates. Kelly Services "bundles the trademarks and trade names with know how and how to officially do temporary staffing services business and then sublicenses it to its foreign affiliates."¹

PETITIONERS' CONTENTIONS

Petitioners contend that Respondent erroneously assessed single business tax liability based on Respondent's determination that certain royalties should have been included in the calculation of Petitioners' sales factor and gross receipts for the 1997 through 2000 tax years.

Petitioners assert that Kelly Properties owns trademarks and trade names and licenses the use of those trademarks and trade names to Kelly Services and other affiliated companies. Kelly Properties also manages the assets used in the business operations of Kelly Services and other affiliated companies. Under the agreements, Kelly Services may subsequently sublicense the trademarks and trade names to foreign affiliated companies and Kelly Services pays the royalty income earned pursuant to those subleases to Kelly Properties. Petitioners assert that neither

¹ Transcript page 6, ll 13-16

Kelly Properties nor Kelly Services sublicense the trademarks or trade names to any unrelated third party.

The revenue at issue is royalty income. Petitioners assert that because the term “royalty” is not defined by the single business tax act, the Courts have looked elsewhere for definitions. In *Mobil Oil Corp v Department of Treasury*, 422 Mich 473; 373 NW2d 730 (1985), the Court adopted *The Random House Dictionary* (rev ed), p 1150 definition of “royalty” which was:

compensation or portion of the proceeds paid to the owner of a right, as a patent or oil or mineral right, for the use of it . . . an agreed portion of the income from a work paid to its author, composer, etc. usually a percentage of the retail price of each copy sold . . . a royal right, as over minerals, granted by a sovereign to a person or corporation . . . the payment made for such a right.

The Court further relied on the following definition from *Black’s Law Dictionary*:

Compensation for the use of property, usually copyrighted material or natural resources, expressed as a percentage of receipts from using the property or as an account per unit produced. A payment which is made to an author or composer by an assignee, licensee or copyright holder in respect to each copy of his work which is sold, or to an inventor in respect of each article sold under the patent. Royalty is a share of product or profit reserved by owner for permitting another to use the property. . . .²

Petitioners cite *Michigan United Conservation Clubs v Department of Treasury*, 239 Mich App 70; 608 NW2d 141 (1999), in which the Court of Appeals held that “. . . a royalty has three key characteristics: ‘(1) it is a payment, (2) in the form of either a product itself or proceeds from the sale of the product, and (3) made in consideration of the use of the property.’” See also, *Detroit Lions, Inc v Department of Treasury*, 157 Mich App 207; 403 NW2d 812 (1986). In *Mourad Bros, Inc v Department of Treasury*, 171 Mich App 792; 431 NW2d 98 (1988), the Court held

² Black’s Law Dictionary (5th ed), page 1195.

that “. . . a royalty is a payment received for the use of property. But it is not a payment for services or a payment for advertising.”

Petitioners contend that Respondent erroneously included the royalties for the use of the trademarks and trade names in the sales factors of both Kelly Services and Kelly Properties.

Petitioners argue that the royalty payments herein involved do meet the definition of sales,³ and thus should not be included in the sales factor for apportionment purposes under section 51⁴ for the tax years at issue. The definition of sales in the single business tax act applicable prior to January 1, 2001, provides:

(1) Sale or ‘sales’ means the gross receipts arising from a transaction or transactions in which gross receipts constitute consideration: (a) for 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, or (b) for the performance of services, which constitute business activities other than those included in (a), or from any combination of (a) or (b).

Petitioners contends that *PM One Ltd v Department of Treasury*, 240 Mich App 255; 611 NW2d 318 (2008), sets forth the appropriate analysis to determine if a transaction constitutes a sale for single business tax purposes. The *PM One* Court broke down the statutory criteria set forth the analysis as follows:

- (1) “gross receipts”
- (2) arising from a “transaction” in which gross receipts constitute ‘consideration’ for one of the following described in (a), (b), or (c):
 - (a) transfer of title to, or possession of, property that is:
 - (i) stock or trade; or

³ Section 7 of the single business tax act (repealed), 1975 PA 228, former MCL 208.7(1)

⁴ Section 51 of the single business tax act (repealed), 1975 PA 228, former MCL 208.51

- (ii) other property of a kind that would be properly included in the inventory of the taxpayer; or
 - (iii) property held by the taxpayer primarily for sale to customers in the ordinary course of its trade or business;
- (b) “performance” of “services,” which constitute “business activities” other than those included in (a); or
- (c) any combination of (a) or (b).

Petitioners argue that based on the definition and above analysis, in order to be included as sales, income must be “consideration for either: (1) the transfer of title or possession of property that is inventory, stock in trade, or property held primarily for sale to customers, or (2) the performance of services.”⁵ Petitioners assert that

royalty transactions do not constitute income from the transfer of title or possession of property that is inventory, stock in trade, or property held primarily for sale to customers. Title to, and possession of, the trademarks and trade names is never transferred. In this case, title and possession . . . remains with Kelly Properties at all times.⁶

Based on these definitions and analyses, the royalty income at issue is not income from a sale and thus not includable in numerator or denominator of either Petitioners’ sales factor.

Petitioners assert that title to, and possession of, the trademarks and trade names are never transferred from Kelly Properties. Petitioners state that “. . . Michigan Courts have held that ‘in order to constitute a sale, absolute ownership over the subject of the transaction must be passed.’” *Detroit Lions, Inc.* Petitioners further rely on *Detroit Lions* for the Court’s opinion that “. . . licensing arrangements that produce royalties result in rights being retained by the

⁵ Petitioner’s brief, page 9

⁶ Petitioners’ brief, page 10

copyright, trademark or trade name owner that are inconsistent with a sale. [Further,] transactions that produce royalties cannot be characterized as a ‘sale.’” *Id.*

Petitioners conclude that, as such, the income in question is definable as royalties and are thus not includable in Petitioners’ sales factor for the tax years at issue.

Petitioners contend that royalties should not be included in gross receipts for the years at issue. Petitioners argue that gross receipts are defined as “the sum of sales, as defined in subsection (1) and rental or lease receipts.”⁷ Petitioners argue that the definition of gross receipts is dependent on and derived from the definition of sales, not the other way around, . . . Any amount excluded from ‘sales’ is therefore excluded from ‘gross receipts’.”⁸ Petitioners assert that royalties do not constitute sales and thus, cannot constitute gross receipts. Petitioners contend that the Court of Appeals “has determined that the categories of ‘rent’ and ‘royalties’ are mutually exclusive.” *Field Enterprises v Department of Treasury*, 184 Mich App 151; 457 NW2d 133 (1990). See also *Columbia Associates, LP v Department of Treasury*, 250 Mich App 656; 649 NW2d 760 (2002). Petitioner states that “[i]n both cases, the Court of Appeals held that the payments were properly characterized as royalties, not rent, and the language of the decisions indicates the two categories are mutually exclusive.”⁹

Petitioners assert that Respondent’s argument that Petitioners are in the business of licensing their intangible property rights is erroneous. Petitioners contend that the business of Kelly Properties is “. . . the management of assets used in the business operations of the Kelly Services

⁷ Petitioner’s brief, page 15

⁸ Petitioners’ brief, page 13

⁹ Petitioner’s brief, page 16

and other affiliated companies.” Additionally, Kelly Properties owns real estate and investments. Kelly Services asserts that its business is “. . . temporary staffing services, not the sale of trademarks or trade names to unrelated third parties.” Kelly Services also bundles the trade names and trademarks with know-how and business techniques that are specific to its temporary staffing business and then licenses this package to its foreign related subsidiaries.

Petitioners also rely on an article Respondent published shortly after the single business tax act was passed that concludes that “. . . because royalty income is specifically excluded from the SBT base, royalty income is also excluded from the apportionment sales factor.”¹⁰ Additionally, Petitioners assert that royalties were specifically excluded from the definition of gross receipts when developing the proposed rules authorized under the single business tax act. See Proposed Rule 208.11. Petitioners argue that, although the proposed rule was never adopted, it still sets forth Respondent’s interpretation of gross receipts and therefore, Respondent cannot change this interpretation without providing proper notice to taxpayers.

Petitioners point out that the single business tax act was amended for tax years beginning after December 31, 2000, to redefine sales and “explicitly provided that royalties received by the taxpayer were not sales.” Petitioners argue that the 2000 amendment makes it clear that sales do not include “royalties received to the extent deducted from the taxpayer’s tax base under section 9(7).”¹¹

¹⁰ Pollack, *Multistate Taxpayers Under the Single Business Tax Act*, 22 Wayne L R 1101, 1006 (1976).

¹¹ Petitioners’ brief, page 14.

RESPONDENT'S CONTENTIONS

Respondent contends that the issue in this matter, as to Kelly Properties is “whether Kelly Properties is eligible for the alternative tax calculation section 31(2) of the single business tax act (repealed), paying tax on 50% of its gross receipts by excluding 95% of its income from its gross receipts. . . . [and] that royalty income from the licensing of intangible personal property rights to Kelly Services must be included in Kelly Properties’ gross receipts.”¹² Respondent asserts that the single business tax act allows a taxpayer to calculate its single business tax liability by applying the tax rate to 50% of its gross receipts and “[t]he addition of the royalty receipts to gross receipts disqualified Kelly Properties from using the gross receipts method of calculating its 1997 SBT.”¹³

Respondent contends that, as to Kelly Services, “royalty income from the licensing of intangible property rights to Kelly Services constitutes sales that must be included in gross receipts and in the calculation of the sales factor.”¹⁴

Respondent contends that the royalties at issue fall within the definition of gross receipts as provided in section 7(1) of the single business tax act (repealed), and as broken down by the Court of Appeals in *PM One Limited, supra*.¹⁵ Respondent further relies on *USX Corp v Department of Treasury*, 187 Mich App 256;466 NW2d 294 (1990), in which the Court held “that receipts from securities sold by the taxpayer were properly excluded from gross receipts where the purchases and sales were not part of the taxpayer’s line of business but were on its

¹² Respondent’s Kelly Properties’ brief, page 1-2

¹³ Respondent’s Kelly Properties’ brief, page 4

¹⁴ Respondent’s Kelly Services’ brief, page 2

¹⁵ See pages 3 and 4 of this Final Opinion and Judgment for the statutory language and Court’s holding in *PM One Ltd*

own account.”¹⁶ Respondent contends that because 95% of Kelly Properties’ income was royalties from the licensing of its intangible property rights, and Kelly Services’ income includes royalties from the licensing of its intangible properties rights, this licensing activity is Petitioners’ “trade or business and the sales occurred in the ordinary course of its trade or business.”¹⁷ Thus, applying *USX*, Respondent contends that the royalties should be included in Petitioners’ sales factors and gross receipts.

Respondent admits that, prior to *Little Caesar Enterprises, Inc v Department of Treasury*, 226 Mich App 624; 575 NW2d 562 (1997), it “treated royalty payments as part of the franchise fee that could not be excluded from the franchisor’s SBT tax base under § 9(7)(c).”¹⁸ The Court “overruled this interpretation,”¹⁹ which resulted in the Department’s review of gross receipts after which the Respondent “correctly determined that where a business’s business activity included franchising, royalty payments constitutes gross receipts.”²⁰

Respondent argues that a sale does not require that title to property transfer; “it is sufficient if possession of the property is transferred and if the property is considered stock in trade or property held by the taxpayer primarily for sale to customers in the ordinary course of its trade or business.”²¹ Respondent contends that as to Kelly Properties, because it licenses the use of trademarks and trade names to Kelly Services and grants Kelly Services the ability to sublicense those rights, “Kelly Services acquires control over property rights and possession is transferred

¹⁶ Respondent’s Kelly Properties’ brief, page 5

¹⁷ Respondent’s briefs, page 5

¹⁸ Respondent’s briefs, page 6

¹⁹ Respondent’s briefs, page 6

²⁰ Respondent’s briefs, page 6

²¹ Respondent’s briefs, page 6

by Kelly Properties. Actual ownership is not necessary for possession.”²² Respondent asserts, as to Kelly Services, that it “licenses related entities to use its properties. Thus, the related entities acquire control over property rights and possession is transferred by Kelly Services.”²³

Respondent argues that actual ownership is not necessary for possession as “long as a person has control or use and enjoyment of property, they have possession of it.” Respondent asserts that the revenue Petitioners receive is consideration for the transfer of the license and the receipts “fall within both the definition of business activity . . . and the definition of sales.”²⁴

Respondent contends that Petitioners’ intellectual property is stock in trade because almost all of Kelly Properties’ business activities consist of the licensing of the property and a portion of Kelly Services’ business activity consists of the licensing of the intellectual property. As such, Respondent asserts that it “. . . correctly required [Petitioners] to include royalties received in its gross receipts and the calculation of the sales factor.”

Respondent states that “[a]lthough the Department issued *internal* bulletins addressing its interpretation of the SBTA, there were no public documents on which the public could rely that would have misled the public or limited the Department’s ability to apply its reinterpretation to all open periods.”²⁵ (Emphasis in original) Respondent asserts that it is not precluded from including Petitioners’ royalty income in gross receipts “since the 1997 instructions also did not indicate that royalty income should be included.”²⁶

²² Respondent’s Kelly Properties’ brief, page 6

²³ Respondent’s Kelly Services’ brief, page 6

²⁴ Respondent’s briefs, page 6

²⁵ Respondent’s briefs, page 7

²⁶ Respondent’s briefs, page 7

Respondent further contends that the amendment to the definition of gross receipts to exclude royalties to the single business tax act and the change in the definition of sales were retroactive but only to years that began after December 31, 2000 and thus not applicable to the tax years here at issue.

PETITIONERS' REPLY IN OPPOSITION TO RESPONDENT'S MOTION
FOR SUMMARY DISPOSITION

In response to Respondent's argument that Petitioners have elected "to pay taxes on '50% of its gross receipts' by electing to use an 'alternative tax calculation,'" ²⁷ Petitioners argue that Respondent is "incorrect" in that there is only one tax base calculated "pursuant to Chapter 3" and the "gross receipts reduction" is taken after the calculation of the adjusted tax base and apportionment factor, "and there is no tax payment on the gross receipts reduction as the Department seems to imply."²⁸ Petitioners assert that Respondent, "in order to avoid the plain language of the statute, has concocted the irrelevant and inapplicable distinction of an 'alternative' method of calculating SBT liability. . . . There is no such 'alternative.'"²⁹ Petitioners further stated that, "[i]f eligible, a taxpayer may, at its option, either take the gross receipts reduction . . . or a compensation reduction. . . . There is nothing gratuitous or benevolent about either procedure."³⁰

Petitioners argue that Respondent's argument that "because 95% of Petitioner's income . . . [was] derived from royalties related to the licensing of its intangible property rights, the royalty income necessarily constitutes a 'sale' and, without offering any support for its assertion,

²⁷ Petitioner Kelly Properties' response brief, page 1

²⁸ Petitioner Kelly Properties' response brief, page 2

²⁹ Petitioner Kelly Properties' response brief, page 2

³⁰ Petitioner Kelly Properties' response brief, page 3

concludes that ‘this is Kelly Properties’ trade or business and the sales occurred in the ordinary course of business . . . [is] an unsupported assertion of fact and unfathomable leap in logic.’³¹

Petitioners further assert that Respondent’s reliance on *USX Corp* is misplaced as *USX Corp* did not involve royalties. Petitioners state that the Court in *USX* did hold that “activities done on the taxpayer’s own behalf could not be sales because the activity was not part of its line of business.”³² Petitioners assert that this supports the exclusion of the royalties as “Petitioner’s licensing of trademarks or trade names similarly was on its own behalf and not part of its management of assets used in the temporary staffing services business of Kelly Services and other affiliated companies.”³³ Petitioner contends that the royalties at issue here are not franchise royalties such that *Little Caesar Enterprises* would apply.

FINDINGS OF FACT

Petitioners are affiliated companies, Kelly Services and Kelly Properties. Kelly Properties manages the assets used in the business operations of Kelly Services and other affiliated companies. Kelly Services is engaged in the business of providing temporary staffing services. Kelly Properties owns and manages trademarks and trade names used solely within Kelly Services’ family of entities. Kelly Properties licenses the use of the trademarks and trade names to Kelly Services. Under the license agreement between Kelly Services and Kelly Properties, Kelly Services has the right to sublicense the trademarks and trade names to its foreign affiliates. Kelly Services bundles the trademarks and trade names with certain know-how and business techniques specific to the temporary staffing business and licenses these to its foreign

³¹ Petitioner Kelly Properties’ response brief, page 4-5

³² Petitioner Kelly Properties’ response brief, page 7

³³ Petitioner Kelly Properties’ response brief, page 8

subsidiaries. The foreign subsidiaries pay royalties to Kelly Services for the use of the trademarks, trade names, and know-how.

For the years at issue, Kelly Services excluded the royalty income received from its foreign subsidiaries from the calculation of the sales factor for apportionment purposes under MCL 208.51 and from the calculation of gross receipts under MCL 208.7(3). For the 1997 tax year, Kelly Properties excluded royalty payments from gross receipts and utilized the gross receipts reduction in calculating its single business tax liability for that year.

The assessment of Kelly Properties is based on Respondent's determination that Kelly Properties is not eligible for a gross receipts reduction for the 1997 tax year and that royalty income attributed to Kelly Properties should be included by Kelly Properties in its calculation of gross receipts for the tax years at issue. The assessment of Kelly Services is based on Respondent's determination that royalty income attributed to Kelly Services should be included by Kelly Services' in its calculation of the sales factor and included in gross receipts.

STANDARD OF REVIEW UNDER MCR 2.116(C)(10)

A motion for summary disposition under MCR 2.116(C)(10) tests the factual support for a claim and must identify those issues regarding which the moving party asserts there is no genuine issue of material fact. Under subsection (C)(10), a motion for summary disposition will be granted if the documentary evidence demonstrates that there is no genuine issue of material fact, and the moving party is entitled to judgment as a matter of law. *Smith v Globe Life Insurance*, 460 Mich 446, 454-455; 597 NW2d 28 (1999). In the event, however, it is determined that an asserted

claim can be supported by evidence at trial, a motion under subsection (C)(10) will be denied.

Arbelius v Poletti, 188 Mich App 14; 469 NW2d 436 (1991).

In *Quinto v Cross & Peters Co*, 451 Mich 358, 362-63; 547 NW2d 314 (1996), the Michigan Supreme Court set forth the following standards for reviewing motions for summary disposition brought under MCR 2.116(C)(10):

In reviewing a motion for summary disposition under MCR 2.116(C)(10), the trial court considers affidavits, pleadings, depositions, admissions and documentary evidence filed by the parties, MCR 2.116(G)(5), in the light most favorable to the party opposing the motion. A trial court may grant a motion for summary disposition under MCR 2.116(C)(10) if affidavits or other documentary evidence show there is no genuine issue in respect to any material fact and the moving party is entitled to judgment as a matter of law. MCR 2.116(C)(10), (G)(4).

The Michigan Supreme Court has established that a court must consider affidavits, pleadings, depositions, admissions, and documentary evidence filed by the parties in the light most favorable to the non-moving party. *Quinto v Cross & Peters Co*, 451 Mich 358, 362-63; 547 NW2d 314 (1996) (citing MCR 2.116(G)(5)). The moving party bears the initial burden of supporting his position by presenting his documentary evidence for the court to consider.

Neubacher v Globe Furniture Rentals, 205 Mich App 418, 420; 522 NW2d 335 (1994). The burden then shifts to the opposing party to establish that a genuine issue of disputed fact exists.

Id. Where the burden of proof at trial on a dispositive issue rests on a nonmoving party, the nonmoving party may not rely on mere allegations or denials in pleadings, but must go beyond the pleadings to set forth specific facts showing that a genuine issue of material fact exists.

McCart v J Walter Thompson, 437 Mich 109, 115; 469 NW2d 284 (1991). If the opposing party fails to present documentary evidence establishing the existence of a material factual dispute, the

motion is properly granted. *McCormic v Auto Club Ins Ass'n*, 202 Mich App 233, 237; 507 NW2d 741 (1992).

CONCLUSIONS OF LAW

The single business tax act does not define the term royalty, although definitions and explanations are provided for certain specific types of royalties and franchise fees.³⁴ The single business tax act does provide that “[a] term used in this act and not defined differently shall have the same meaning as when used in comparable context in the laws of the United States relating to federal income taxes in effect for the tax year unless a different meaning is clearly required.”³⁵

The Michigan Supreme Court discussed the definition of royalties in the context of the single business tax act in several cases. In *Zenith Data Systems Corp and Health Co, Inc v Department of Treasury*, 218 Mich App 742; 555 NW2d 264 (1966), the Court of Appeals held that there was no definition of royalty in the federal tax law used in a directly comparable context to the single business tax act.³⁶ *Mobil Oil Corp, supra* at 484; and *Town & Country Dodge, supra* at 239-240.

The Supreme Court in *Mobil Oil Corp*, looked to extrinsic sources, including dictionaries, to help discern the meaning of the term royalties as used in the single business tax act.³⁷ Further, the Courts³⁸ are clear that the key characteristics of a royalty is that, “(1) it is a payment, (2) in the form of either a product itself or proceeds from the sale of the product, and (3) made in consideration of the use of the property.”

³⁴ MCL 208.9(4)(g) and MCL 208.9(7)(c)

³⁵ MCL 208.2(2)

³⁶ See also *Mobil Oil, supra* at 484; and *Town & Country Dodge*

³⁷ See page 3

³⁸ *Michigan United Conservation Clubs v Department of Treasury*, 239 Mich App 70, 79; 608 NW2d 141 (1999)

The receipts involved in this matter are royalties. They easily fit within the definitions used by the Court in *Mobil Oil*. The income is “compensation or portion of the proceeds paid to the owner of a right”³⁹ and “compensation for the use of property, usually copyrighted material . . . a share of product or profit reserved by owner for permitting another to use the property.”⁴⁰ Specifically, the payments received are proceeds from the licensing to affiliated companies of Kelly Properties and Kelly Services’ trade names and trademarks. Further, the income is in consideration of the use of the companies’ brand name and trademarks. Respondent does not contest that the income involved are royalties. Respondent refers to the income as royalties or royalty receipts. However, Respondent asserts that the royalties arise from sales and, as such, are includable in Petitioners’ gross receipts and sales factors.⁴¹

Section 7(1) of the single business tax act, in effect for the tax year at issue, defined sales as:

[T]he gross receipts arising from a transaction or transactions in which gross receipts constitute consideration: (a) for 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, or (b) for the performance of services, which constitute business activities other than those included in (a), or from any combination of (a) or (b).

The Court of Appeals in *PM One Ltd v Department of Treasury*, 240 Mich App 255, 261; 611 NW2d 318 (2000), set out the appropriate way to analyze what constitutes sales.⁴² The Court of Appeals in *Detroit Lions, Inc v Department of Treasury*, 157 Mich App 207, 217; 403 NW2d 812 (1986), stated that “. . . in order to constitute a sale, absolute ownership over the subject of

³⁹ *The Random House Dictionary* (rev ed), p 1150

⁴⁰ Black’s Law Dictionary (5th ed), page 1195

⁴¹ Only Kelly Services’ petition alleges there is an issue as to whether royalties must be excluded from the calculation of the numerator and the denominator of the sales factor. Petitioners’ petition, p 11.

⁴² See page 4

the transaction must be passed.” (citing *Central Discount Co v Department of Revenue*, 355 Mich 463, 467; 94 NW2d 805 (1959)). In *Detroit Lions*, a licensing agreement was set up between television networks and the football team in regard to live sports broadcast rights. The Court determined the payments were royalties and not includable in the tax base because the licensing arrangement that produced the royalties resulted in rights being retained by Petitioner that was inconsistent with a sale. *Id.* at 218-219.

In applying the *PM One Ltd* analysis, the Tribunal must determine if all the criteria have been met. The “gross receipts” must have arisen from a “transaction” in which the gross receipts constituted “consideration” for one of the specifically enumerated actions. Respondent asserts that based on its determination that “95% of Kelly Properties’ income was royalties from the licensing of its intangible property rights. . . .clearly this is Kelly Properties’ trade or business and the sales occurred in the ordinary course of its trade of business.”⁴³ However, Respondent offers no support for this conclusion or any testimony that contradicts the affidavit of Michael F. Orsini to the contrary. Petitioners have provided support for their position that this was not Petitioners’ primary business. Respondent must do more than boldly state its disagreement with Petitioners’ position to carry its burden.

The Tribunal is unconvinced by Respondent’s argument that Petitioners transferred possession of the “property.” Kelly Properties retains ownership of the trademarks and trade names at all times.⁴⁴ Regardless of how many times Kelly Services was allowed to use those trademarks and trade names, Kelly Services did not control the use of the trademarks or trade names beyond so

⁴³ Respondent’s brief, page 5

⁴⁴ Affidavit of Michael F Orsini, paragraph 12, page 2.

as to impact in any way the property rights of Kelly Properties. Kelly Properties remained the owner of that property and could further allow the use or not, at its discretion. Kelly Properties gave up no property rights by allowing Kelly Services to use the trademarks and trade names. And further, if Kelly Services was allowed to sublicense the trademarks and trade names, Kelly Properties still retained full ownership rights to that property. And, whether used by Kelly Properties, Kelly Services, or other affiliated companies, the trademarks and trade names were used solely within the Kelly Services' family of entities. The licensees, Kelly Services and its foreign affiliates, merely compensate the licensor for use of the intangible property. This falls squarely within the Court of Appeals conclusion that a royalty is a payment received for the use of property. *Mourad Bros, supra* at 796 (citing *Mobil, supra* at 485).

Respondent argues that Petitioners' royalty receipts fall within the Court's definition of sales in *PM One Ltd* and relies on the rule from the *USX Corp* case⁴⁵ to support its conclusion that licensing its intangible property rights is part of Petitioners' trade or business and therefore occurred in the ordinary course of its trade or business. Respondent extends its argument by asserting that the trademarks and trade names are stock in trade or property of a kind that would be properly included in the inventory. Further, Respondent argues that it is not required that title to property transfer or the property be tangible or real and that possession of Petitioners' trade names and trademarks transfers to the licensee when used making the royalty income gross receipts. The Tribunal finds that Petitioners' intangible trademarks and trade names are not held as inventory or other property primarily for sale to customers.⁴⁶ The Tribunal finds that, contrary

⁴⁵ "*USX* held that receipts from securities sold by the taxpayer were properly excluded from gross receipts where the purchases and sales were not part of the taxpayer's line of business but were on its own account." Respondent's Brief in Opposition to Plaintiff's Motion for Summary Disposition at page 5.

⁴⁶ Affidavit of Michael F Orsini, paragraph 13, page 2.

to Respondent's argument, Michigan's case law holds that royalties and sales are mutually exclusive. Petitioners are not in the business of selling their intangible rights but rather Petitioner Kelly Properties is in the business of managing the buildings, investments, trademarks, and trade names on behalf of the affiliated companies and does not involve the sale of trademarks or trade names to unrelated third parties of staffing of temporary services for its customers' businesses⁴⁷ and Petitioner Kelly Services is in the business of temporary staffing services.⁴⁸

Notwithstanding the above, the Tribunal finds that, based on the facts and evidence presented, the trademarks and trade names were not "stock or trade" and were not held in inventory for sale to customers. Nor did Respondent offer any plausible analysis to support a finding that the use of the trademarks was the "performance of services."

The Tribunal does not find that Petitioners' argument related to a passage from *Multistate Taxpayers Under the Single Business Tax Act* provides precedential or reliable support for its position. Further, Petitioners' reliance on an internal memorandum is flawed. In *Kmart Michigan Property Services, LLC v Department of Treasury*, 283 Mich App 647; 770 NW2d 915 (2009), lv den 485 Mich 898, the Court found that ". . . the Department of Treasury may periodically issue bulletins which index and explain current department interpretations of current state tax laws. A bulletin issued by the Department of Treasury does not have the force of law. Although not legally binding, an administrative bulletin reflects the interpretation of tax statutes given by the agency charged with their enforcement, and is entitled to respectful

⁴⁷ Affidavit of Michael F Orsini, paragraph 15, page 2.

⁴⁸ Affidavit of Michael F Orsini, paragraph 14, page 2.

consideration.”⁴⁹ Here, Petitioners ask the Tribunal to rely on an internal memorandum, not a revenue bulletin which is a public document, which is afforded even less deference. Petitioners also offer Proposed Rule 208.11, which specifically excluded royalties from the definition of gross receipts, in support of its position. Proposed rules are not legally binding nor precedential such that the Tribunal should rely on them.

Petitioners argue that royalties, because they are not sales, are not included in gross receipts for the tax years at issue. Section 7 of the single business tax act, as in effect for the tax years at issue, defined the term “gross receipts” as follows:

(3) “Gross receipts” means the sum of sales, as defined in subsection (1) and rental or lease receipts. Gross receipts does not include the amounts received in an agency or other representative capacity, solely on behalf of another or others but not including amounts received by persons having the power or authority to expend or otherwise appropriate such amounts in payment for or in consideration of sales or services made or rendered by themselves or by others acting under their direction and control or by such fiduciaries as guardians, executors, administrators, receivers, conservators, or trustees other than trustees of taxes received or collected from others under direction of the laws of the federal government or of any state or local governments.

The Court of Appeals in *PM One Ltd* held that the definitions of sales and gross receipts are circular stating, “. . . given this somewhat circular definition, what constitutes gross receipts depends largely on the meaning of ‘sales’ in the SBTA.” The Tribunal has concluded that the royalty income at issue is not sales. The second prong of the definition of the gross receipts would include rental or lease receipts. The Court of Appeals has held that “. . . [certain]

⁴⁹ The legislature enacted MCL 205.6a which revised this rule. The statute states that, “[a] taxpayer may rely on a bulletin or letter ruling issued by the department after September 30, 2006 and shall not be penalized for that reliance until the bulletin or letter ruling is revoked in writing. However, that reliance by the taxpayer is limited to issues addressed in the bulletin or letter ruling for tax periods up to the effective date of an amendment to the law upon which the bulletin or letter ruling is based or for tax periods up to the date of a final order of a court of competent jurisdiction for which all rights of appeal have been exhausted or have expired that overrules or modifies the law upon which the bulletin or letter ruling is based.” This amendment was not in effect for the tax years at issue.

payments were properly characterized as royalties, not rent, and the language of the decisions indicates the two categories are mutually exclusive.” See *Field Enterprises* and *Columbia Associates, supra*. The Tribunal previously determined that the income at issue are royalties. Applying the holdings in *Field* and *Columbia*, the Tribunal finds that the relevant income cannot be royalties and rents. The royalty income is rental or lease receipts and is therefore not gross receipts.

Petitioner, Kelly Services, argues that Respondent included intercompany transfers in the gross receipts and sales factors. Kelly Services alleges that Respondent sent Kelly Services several letters advising it that the intercompany transactions are eliminated from gross receipts and sales factor apportionment when filing a consolidated SBT tax return.⁵⁰ See also section 77 of the single business tax act. Respondent does not contest Petitioners’ assertion that the intercompany transactions were “inadvertently included in the 2000 assessment,”⁵¹ and stated that “those should be removed.”⁵²

The Tribunal finds that there is no genuine issue as to any material fact and that, as such, summary disposition is appropriate in this matter. Further, the Tribunal has considered the affidavits, pleadings, depositions, admissions, testimony, and documentary evidence filed by the parties, MCR 2.116(G)(5), and in the light most favorable to the party opposing the motion, finds that Petitioners’ Motions for Summary Disposition should be granted.

More specifically, as to Kelly Properties, the Tribunal finds that,

⁵⁰ Exhibits 5 and 14.

⁵¹ Transcript page 30, ll 17-18

⁵² Transcript page 30, ll 18-19

1. The amount of royalties based on intercompany transactions between Petitioners should be excluded from the calculation of the numerator and denominator of the sales factor.
2. The amount of royalties should be excluded from the calculation of gross receipts for the tax years at issue.

As to Kelly Services, the Tribunal finds that

1. The amount of royalties based on intercompany transactions between Petitioners should be excluded from the calculation of the numerator and denominator of the sales factor.
2. The amount of royalties should be excluded from the calculation of gross receipts for the tax years at issue.

Further, consolidation is appropriate in view of the common issues of fact and law involved.

JUDGMENT

IT IS ORDERED that MTT Docket Nos. 319360 and 319361 are CONSOLIDATED.

IT IS FURTHER ORDERED that Petitioners' Motion for Summary Disposition is GRANTED.

IT IS FURTHER ORDERED that Respondent's Motion for Summary Disposition is DENIED.

IT IS FURTHER ORDERED that Respondent's Final Bill for Taxes Due, Assessment No.

L743510, dated June 9, 2005, for tax years 1997 through 2000 is CANCELLED.

IT IS FURTHER ORDERED that Respondent's Final Bill for Taxes Due, Assessment No.

L755152, dated June 9, 2005, for tax year 1997 is CANCELLED.

This Opinion and Judgment resolves all pending claims in this matter and closes this case.

MICHIGAN TAX TRIBUNAL

Entered: August 26, 2010

By: Rachel Asbury