STATE OF MICHIGAN

COURT OF CLAIMS

AAA LIFE INSURANCE COMPANY,

Plaintiff,

v

DEPARTMENT OF TREASURY, STATE OF MICHIGAN,

Defendant.
_____/

OPINION AND ORDER

Case No. 21-000242-MT

Hon. Brock A. Swartzle

The sole question in this action is whether plaintiff, a Michigan company, "used" direct-mail advertisements that an out-of-state company prepared and mailed on plaintiff's behalf, rendering the transactions taxable under the Use Tax Act (UTA), MCL 205.91 *et seq*. Plaintiff contends that it relinquished any control over the advertisements before their distribution in Michigan. Defendant argues that plaintiff retained some level of control over the advertisements from the development phase through their distribution. Both parties have moved for summary disposition under MCR 2.116(C)(10). The Court has reviewed the briefing and dispenses with oral argument. The Court concludes that plaintiff retained a sufficient level of control over the advertisements in Michigan for the use tax to apply here. Consequently, the Court GRANTS defendant's motion for summary disposition and DENIES plaintiff's motion for summary disposition.

I. BACKGROUND

Plaintiff is a life-insurance company headquartered in Livonia, Michigan. Plaintiff sells three products: (1) direct-term life insurance; (2) member-loyalty travel accident insurance; and (3) guaranteed whole-life insurance. Plaintiff conducts 13 mail advertisement campaigns each year, at a rate of about one campaign every 28 days. The campaigns advertise two products, one of which is always the direct-term life insurance. The advertising package generally consists of a brochure, an application for the life-insurance product, a letter, and a business-reply envelope. Plaintiff distributes somewhere between 160,000,000 and 200,000,000 advertisements (also known as direct-mail packages) through the mail each year.

Since 1999, plaintiff has contracted with a Missouri marketing company, American Direct Marketing Resources, LLC (ADMR), to process, print, and deliver the advertisements to the United States Postal Service (USPS) for distribution. Plaintiff and ADMR have operated under the same contract since 2014. Section 1 of plaintiff's contract with ADMR outlines the services that ADMR has agreed to provide in relation to the direct-mail marketing campaign, such as creating package proofs and releasing materials to a third-party printer. In Section 2 of the contract, plaintiff agrees to pay ADMR for its services based on purchase orders that ADMR submits to plaintiff.

The contract also explains the different items for which ADMR may charge plaintiff, which includes the packages themselves, as well as postage and other mailing costs. Section 6 of the contract, which governs ownership, explains, "Contractor shall own exclusive rights and costs associated to [sic] the creation and use of all creative packages developed under this Agreement." Yet the same provision grants plaintiff the authority to reject any packages: "Client is under no obligation to purchase or use any packages developed under this Agreement." According to

ADMR President Ed Smith, ADMR has exclusive ownership rights over the creative packages and places its copyright seal on the advertisements.

Section 4 of the contract, which governs warranties, states, in relevant part, "Client reserves the right, in its sole discretion, to determine whether the services provided meet with Client's reasonable satisfaction. Contractor shall present to Client final proofs of all advertising materials for Client's approval prior to printing. Client approval of proofs is authorization to Contractor to print as proofed." In Section 8, plaintiff retains ownership over any information about its members or their families, which ADMR agrees is "proprietary and highly confidential." Finally, Section 12 of the contract is a merger clause, which states in relevant part, "This Agreement contains the entire understanding of the parties related to the subject matter of this agreement."

As plaintiff's representatives explained in their depositions, the process for developing the advertisements begins with a brainstorming session about the topic of the campaign, which usually occurs at plaintiff's office in Livonia. During those meetings, plaintiff and ADMR's representatives discuss new campaigns, new concepts, business objectives, and scheduling. ADMR then develops an advertisement draft after receiving a "creative brief" (or concept brief) outlining the theme of the new advertisement (according to plaintiff, ADMR sometimes prepares the creative brief itself). ADMR creates a base package (or a digital proof) reflecting the concepts outlined in the creative brief. Jennifer Hart, plaintiff's Vice President of Direct Digital & Data and Analytics, acknowledged in her deposition that, during this stage, plaintiff may make a "few iterations of approval" for accuracy and to ensure that the base package is in line with the concepts in the creative brief.

Plaintiff will also review ADMR's work product through an online application called Aproove. In this stage, plaintiff retains the ability to insist that language appear (or not appear) in the advertisements, but sometimes defers to ADMR's expertise. As Hart explained, "It is a collaboration and collective output." She agreed, however, that the decision whether to mail the packages is "ultimately something that's within AAA's control." The Aproove review also includes a level of compliance, as plaintiff must ensure that any rate charts and other state-insurance information in the package are correct. As Becky Quinlan, plaintiff's Director of Direct Mail Creative and Operations, explained in her deposition, "We are ultimately responsible to make sure that the approvals are correct, and we—we have the right to go back and say this is not correct."

As this process is happening, plaintiff's data-analytics team (which includes three or four Livonia-based employees) determines the target audience for the campaign. To identify target customers, plaintiff analyzes data that, during the audit period at issue, was provided by a Texas data-hosting company called Wunderman Thompson (plaintiff now uses a different data-hosting company). After Wunderman Thompson "cleansed" and reviewed the data, plaintiff selected the target audience based on a "predictive model score" developed by its data scientists. Wunderman Thompson sent the data to ADMR, and plaintiff never had that data in its possession. Nor did plaintiff have rights to the data Wunderman Thompson hosted.

Once plaintiff approves the final proofs for the advertisements, ADMR fulfills the printing through third-party vendors based outside of Michigan. ADMR provides plaintiff with progress reports during the printing stage. Plaintiff concedes that it "may have informational and informal touchpoints" with ADMR during the printing process, which become less frequent over time. Hart submitted an affidavit in support of plaintiff's motion for summary disposition, in which she states

that plaintiff "rarely takes action in response to these touchpoints with ADMR, only in specific circumstances if needed."

When the advertisements are printed, ADMR ships the advertisements through USPS. The postage statement for the advertisements states that plaintiff is both the "Permit Holder" for the advertisements and the individual or organization for which the mailing is prepared. Plaintiff's employees receive copies of the advertisements in the mail to determine whether ADMR mailed the advertisements properly and the length of delivery from USPS. If there is an issue with the advertisements, then plaintiff will perform a root-cause analysis and may require ADMR to issue a corrected mail package.

After plaintiff submitted its tax returns for tax years 2016-2018, defendant conducted a use-tax audit and determined that plaintiff owed use tax for the portion of the advertisements allocated to Michigan. In 2020, defendant issued Intents to Assess Nos. VA6KC5R, VA6kC5S, and VA6KC5T. Plaintiff challenged defendant's conclusion and requested an informal conference. During the February 2021 informal conference, plaintiff argued that it had no control over the advertisements in Michigan because it ceded any control before the mail was delivered to the USPS outside of Michigan. Defendant argued, in contrast, that plaintiff continued to exercise control over the advertisements by directing where ADMR sent the mail. While a decision was pending, plaintiff paid the use tax under protest. Following the hearing, the referee, Sherry Hilpert, concluded that plaintiff exercised no right or control over the advertisements after ADMR transported them to USPS locations out of state. Plaintiff had no control over when, how, or even if the mail would be delivered to Michigan residents. So Hilpert recommended that defendant eliminate the use-tax assessment.

Defendant, however, reversed that determination, concluding that plaintiff was involved in key aspects of the production and distribution under the terms of its contract with ADMR. Defendant pointed to the language in the contract allowing plaintiff to determine whether it was reasonably satisfied with ADMR's services, and providing that plaintiff's approval of the final proofs served as authorization to begin printing. Defendant found that the key factor was that plaintiff was a Michigan-based company directly engaging and controlling transactions within Michigan. Defendant also found persuasive the fact that information about plaintiff's members and their families remained the sole property of plaintiff or its related AAA clubs. Defendant concluded that plaintiff "retained and exercised sufficient control over the Direct Mail *in Michigan*, as [plaintiff] is headquartered and has its principal place of business in Michigan, so that its actions (e.g., sign-offs and approvals) occurred in Michigan, to constitute a taxable us under the Use Tax Act." Defendant issued Final Assessments for the 2016-2018 tax years.

Plaintiff then sued in this Court and, after some discussion with defendant about a perceived mathematical issue with the Final Assessments, filed a first-amended complaint. In Count I, plaintiff asserts that there was no taxable use of the direct-mail materials during the relevant tax years. Plaintiff alleges that it "ceded all control" over the advertisements to ADMR. In Count II, plaintiff alleges that the direct-mail statutes, such as MCL 205.71a, do not impose a use tax in this circumstance. Both parties have moved for summary disposition. In its motion, defendant emphasizes that plaintiff exercised significant control over the advertisements, which were purchased outside of Michigan but then were distributed in Michigan. Plaintiff argues in its motion that it relinquished control over the advertisements before they became tangible property and before they were disbursed in the state, meaning that plaintiff never had control over tangible personal property. Plaintiff argues that any of its residual activities after the advertisements are

distributed do not constitute control over the advertisements. Plaintiff does not present an argument about the direct-mail statutes in its briefing.

II. ANALYSIS

Both parties request summary disposition under MCR 2.116(C)(10). Summary disposition is appropriate under MCR 2.116(C)(10) when "there is no genuine issue with respect to any material fact and the moving party is entitled to judgment as a matter of law." *Emagine Entertainment, Inc v Dep't of Treasury*, 334 Mich App 658, 663; 965 NW2d 720 (2020) (cleaned up). The Court examines the documentary evidence to determine whether, after drawing all reasonable inferences in favor of the nonmovant, a genuine issue of material fact exists. *Id.* "A question of fact exists when reasonable minds could differ as to the conclusions to be drawn from the evidence." *Id.* (cleaned up).

To the extent the Court is required to interpret the UTA, the goal of statutory interpretation is to give effect to the intent of the Legislature. *Badeen v PAR, Inc.* 496 Mich 75, 81; 853 NW2d 303 (2014). The focus is on the express (or plain) language of the statute, which must be considered in the context of the entire statute. *Id.* Only when there is an ambiguity in the plain language of a tax statute will the Court engage in judicial construction of the statute. *Zug Island Fuels Co, LLC v Dep't of Treasury*, ___ Mich App ___; ___ NW2d ___ (2022) (Docket No. 356419); slip op at 4.

The UTA levies a 6% tax on individuals who enjoy "the privilege of using, storing, or consuming tangible personal property" in the state. MCL 205.93(1). The use tax compliments sales tax and is designed to govern transactions that are not subject to sales tax. *Podmajersky v Dep't of Treasury*, 302 Mich App 153, 162-163; 838 NW2d 195 (2013). The UTA defines the

term "use" to mean "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." MCL 205.92(b). A person is liable for use tax if the individual exercises some rights of ownership in Michigan, which is demonstrated by having "some level of control" over the property. *Auto-Owners Ins Co v Dep't of Treasury*, 313 Mich App 56, 70; 880 NW2d 337 (2015). The distribution of property constitutes a use under the UTA if the owner exercises a right or power incident to ownership while the property is in Michigan. *Ameritech Publishing, Inc v Dep't of Treasury*, 281 Mich App 132, 139; 761 NW2d 470 (2008). The standard for exercising some level of control is broad, and even the act of ceding control over property may constitute a right incident to ownership. See *NACG Leasing v Dep't of Treasury*, 495 Mich 26, 30-31 & n 16; 843 NW2d 891 (2014) (executing a lease in Michigan is an exercise of a right incident to ownership). Finally, "tangible personal property" is defined as "personal property that can be seen, weighed, measured, felt, or touched or that is in any other manner perceptible to the senses and includes electricity, water, gas, steam, and prewritten computer software." MCL 205.92(k).

The parties agree that the most relevant published cases concerning the use-tax implication of distribution of tangible property in Michigan are *Sharper Image Corp v Dep't of Treasury*, 216 Mich App 698; 550 NW2d 596 (1996), and *Ameritech*, 281 Mich App 132. But the parties dispute which of these two cases should apply in this context. The Court will examine each case in turn. Starting with *Sharper Image*, the plaintiff in that case was a foreign corporation that owned two Michigan stores and conducted business in Michigan through mail-order catalogs. *Sharper Image*, 216 Mich App at 700. A third-party vendor in Nebraska printed and shipped the mail-order catalogs. *Id.* The plaintiff retained no control over the catalogs after the third party delivered them to the postal service for shipment. *Id.* The defendant (the Department of Treasury) issued a use-

tax deficiency on the plaintiff's tax returns for use of the catalogs, and the plaintiff sued after paying the amount due under protest. *Id.*

After the Court of Claims granted summary disposition in the defendant's favor, the plaintiff appealed, arguing that the term "use" in the UTA does not include the distribution of catalogs from an out-of-state source. *Id.* at 700-701. The Court of Appeals agreed. *Id.* at 701. The Court concluded that the plaintiff's exercise of power over the catalogs ended when they were delivered to USPS in Nebraska. *Id.* at 702. The Court also concluded that the UTA definition of "use" did not allow the Department to tax the distribution of catalogs. *Id.* at 703. The Court distinguished the situation from caselaw from other states, where the taxpayer had enjoyed "indicia of control" over the advertisements, such as the power to determine in what publications the advertisements would be placed and when they would be distributed. *Id.* at 704.

In contrast, in *Ameritech*, 281 Mich App at 133-134, the plaintiff published and distributed telephone directories to customers in Michigan. Another entity printed and prepared the directories at an Illinois facility. *Id.* at 134. The plaintiff would first develop the content included in the directories, providing it to the Illinois company in an electronic format, then the plaintiff purchased the paper to print the directories from non-Michigan factories. *Id.* The plaintiff contracted with a carrier to transport the directories from the Illinois facility, and a product-development corporation to distribute the directories. *Id.* After the defendant denied the plaintiff's use-tax refund request, the Court of Claims upheld that decision, and the plaintiff appealed. *Id.* at 135.

On appeal, the Court of Appeals clarified its holding in *Sharper Image* and explained that the distribution of tangible personal property is a "use" under the UTA if the owner exercised a

right or power incident to ownership while the property was located in Michigan. *Id.* at 139. The owner no longer has a right or power to the property if it has "ceded total control" over the property to another party. *Id.* at 140. The Court reviewed the carrier and distributer contracts, and determined that the plaintiff did not cede total control over the directories. *Id.* at 141. The plaintiff maintained control over the scheduling of the printing and distribution of the directories, as well as the method by which the distributer delivered the directories. *Id.* at 141-142. The plaintiff's control extended to the dates of distribution and the quality-assurance program that the distributer was to implement. *Id.* at 143-144. The distributer was also required to report to the plaintiff about the progress of the delivery. *Id.* at 143. And, at the end of the distribution cycle, all remaining directories were the plaintiff's property and were disposed of at the plaintiff's recycling supplier. *Id.* Based on all this evidence, the Court concluded that the plaintiff never lost all control over the directories. *Id.* at 144.

The Court of Appeals most recently addressed the use-tax implications for delivering advertisements in Michigan in *Bed Bath & Beyond Inc v Dep't of Treasury*, unpublished per curiam opinion of the Court of Appeals, issued July 8, 2021 (Docket Nos. 352088 and 352667).[1] In *Bed Bath & Beyond*, the Court of Appeals determined that the plaintiff did not use advertising materials in Michigan because it retained no control over the delivery process after sending the paper materials to a third-party vendor. *Id.* at 11-12. The plaintiff was a New Jersey company with 31 stores in Michigan. *Id.* at 1. The plaintiff designed the advertising materials outside the state of Michigan. *Id.* Then, the plaintiff would purchase the paper product and send it to a third-party

[1] Although unpublished, *Bed Bath & Beyond* may hold persuasive value. See MCR 7.215(C)(1); *Haydaw v Farm Bureau Ins Co*, 332 Mich App 719, 726 n 5; 957 NW2d 858 (2020).

printer outside of Michigan. *Id.* at 1-2. After the advertisements were printed, the plaintiff had the printer send them to a mail vendor known as Harte Hanks Mailing House, which was also located outside of Michigan. *Id.* at 2. Harte Hanks's contractual obligations included to process and prepare the advertisements for mailing to the plaintiff's customers through the USPS. *Id.* Harte Hanks printed addresses on the advertisements through an "audience file" owned by Harte Hanks, and sorted the advertisements for mailing. *Id.* The plaintiff paid Harte Hanks for its freight-service costs. *Id.*

After engaging in a detailed analysis of both *Sharper Image* and *Ameritech*, the *Bed Bath & Beyond* panel concluded that the case was analogous to *Sharper Image*. *Id.* at 10. The panel found persuasive the fact that the advertisements were produced outside of Michigan and that Harte Hanks had complete control over the preparation and delivery of the advertisements within Michigan. *Id.* And although the plaintiff had specified the Michigan residents to whom Harte Hanks should mail the materials, Harte Hanks developed its own audience file to use in distributing the materials. *Id.* Indeed, the only indicia of control were providing a list of customers to Harte Hanks and directing the dates of distribution, but neither of these things involved control over the process of delivery. *Id.* at 11. The panel simplified its holding as follows: "We . . . conclude that an absence of control over the materials within the state's borders makes the distribution nontaxable, while some or any control over the materials within the state's borders makes the distribution taxable." *Id.*

Defendant relies on Judge MARKEY's partial concurrence and partial dissent as persuasive authority. Judge MARKEY concluded that the plaintiff had exercised a right incident to ownership by contracting with Harte Hanks and requiring Harte Hanks to deliver the materials within certain parameters. *Bed Bath & Beyond*, unpub op at 3 (MARKEY, P.J., concurring in part and dissenting

in part). Also, because the plaintiff had directed Harte Hanks to deliver the advertisements to Michigan residents, the plaintiff exercised a right of control in Michigan until the advertisements entered the USPS facilities. *Id.* The materials remained the plaintiff's property until they were delivered. *Id.* The sole exception, in Judge MARKEY's view, was for smaller campaigns in which Harte Hanks delivered the advertising materials to a USPS facility outside of Michigan. *Id.*

One critical distinction between this case and the cases discussed above is that plaintiff is headquartered in Michigan, and the development of its direct-mail campaign, as well as its purchase of ADMR's services and materials, occurred in this state. *Sharper Image* and *Bed Bath & Beyond* focused on distribution because the taxpayers were located out of state, and distribution was the only in-state activity (the Court of Appeals did not state where the plaintiff in *Ameritech* was located). In contrast, plaintiff maintains its headquarters in Michigan, and this is where plaintiff engaged with ADMR about the advertisements. Because plaintiff's headquarters is in Michigan, the Court's review of plaintiff's control over the property within the state is not limited to the distribution of the advertisements.

Plaintiff's primary argument is that once it approved the digital design of the advertisements (which it characterizes as intangible products), ADMR owned the creative rights to any physical advertisement it produced. So, in plaintiff's view, it never exercised any ownership-type right over the tangible property because ADMR owned the creative rights to the advertisements and handled all printing and distribution activities. But the UTA does not restrict application of use tax to only the personal property over which the taxpayer holds legal title or copyright. See *Auto-Owners*, 313 Mich App at 72-73 (holding that the plaintiff exercised an ownership right over print resource materials it received from a publishing company without

reference to copyright). The test is much less stringent and examines whether the taxpayer exercised sufficient level of control over the property in the state. See *id.* at 70.

Here, even though the parties' contract contemplated that ADMR would retain creative rights and copyright over the contents of the advertisements, plaintiff exercised at least some level of control over the advertisements in this state. There is no doubt that the purpose of the advertisements is to promote plaintiff's life-insurance products to existing and potential customers. Nevertheless, plaintiff argues that its involvement in the process is limited to (1) developing the content of the advertisements with its creative partners; and (2) scheduling the advertising campaigns for each calendar year. But plaintiff retains far more control than simply directing the message. Among other things, under the terms of the contract, ADMR must obtain plaintiff's approval for the final proofs before they are printed, and plaintiff has the authority to insist on changes to the message if the proofs do not meet with plaintiff's reasonable satisfaction. Plaintiff also reviews the proofs for compliance with insurance laws and to ensure that they contain accurate rates. And plaintiff has the final say in whether ADMR mails the advertisements.

Even after ADMR begins to process the advertisements, plaintiff retains some level of control. Unlike the situation in *Bed Bath & Beyond*, ADMR does not have control over the "audience file" for the mailers—plaintiff provides the list of recipients with the assistance of another third party. Once ADMR mails the advertisements (identifying plaintiff as the Permit Holder), plaintiff receives a copy in the mail and can require ADMR to send a corrected mail package if there is a mistake in the original. Plaintiff retained some measure of control over the advertisements even during their distribution. The Court concludes, therefore, that plaintiff retained at least some level of control over the advertisements in Michigan at all relevant phases

of the production and distribution process, rendering its use of the advertisements a taxable use under the UTA.

Finally, the Court notes that plaintiff alleges in its amended complaint that defendant's Final Assessments contained a mathematical error because defendant improperly credited plaintiff's payment toward the 2016-2017 tax years, only, and not to each of the tax years at issue. Neither party has addressed that issue on summary disposition, however, and the Court declines to address this unbriefed issue.

III. CONCLUSION

For the reasons stated in this Opinion and Order, IT IS ORDERED that defendant's motion for summary disposition is GRANTED.

IT IS FURTHER ORDERED that plaintiff's motion for summary disposition is DENIED.

IT IS SO ORDERED. This is a final order that resolves the final claim and closes the case.

Dated: January 12, 2023

Hon. Brock A. Swartzle
Judge, Court of Claims