NOTICE TO TAXPAYERS REGARDING
AUTO-OWNERS INSURANCE COMPANY v DEPARTMENT OF TREASURY

Issued: January 6, 2016

I. Impact of *Auto-Owners Insurance Company v Department of Treasury*

On October 27, 2015, the Michigan Court of Appeals issued a decision in *Auto-Owners Insurance Company v Department of Treasury*[1] ("*Auto-Owners*"). At issue in *Auto-Owners* was whether certain products were subject to the imposition of use tax on prewritten computer software delivered in any manner under MCL 205.92b(o).

The Court of Appeals found in favor of Auto-Owners. Essentially, the court found that there were two different categories of products at issue in the case.

One category consisted of products that did not include the delivery of "code that enabled" the vendor's system to operate. The court found these products did not satisfy the requirement that prewritten computer software must be delivered, in any manner, because there was no proof that code was electronically delivered to Auto-Owners, or that Auto-Owners exercised any incidence of ownership over the vendor's code. Specifically, the court held that:

> The majority of the transactions in this case were not taxable under the UTA because they did not involve the delivery of prewritten computer software by any means. With regard to West, plaintiff never exercised an ownership-type right or power over any West computer software. Instead, all the code remained on West's server. West controlled the code, maintained it, and updated it as it saw fit. Plaintiff only accessed a website that allowed it to submit requests to the West system that controlled the code. Accessing West's code in such a limited manner is not an exercise of a right or power over the code incident to the ownership of that code because accessing the code in such a limited manner does not signify ownership. Therefore, plaintiff did not use tangible personal property with regard to West.[2]

The second category consisted of products where the court found that some prewritten computer software was electronically delivered to Auto-Owners. The court found that the electronic delivery of a "local client" or "desktop agent" was sufficient to constitute an "ownership-type right" over the product. The court held:

> With regard to LogMeIn, plaintiff used a remote access agent that LogMeIn supplied and that was necessary to run locally on plaintiff's machines in order to access the network and its features. The local client, or desktop agent, was installed on each computer. The desktop agent constituted prewritten computer software since it included a set of coded instructions designed to cause the computer to perform a task. See MCL 205.92b(c). The software was delivered since plaintiff had actual possession of the desktop agents.[3]

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[1] ___ Mich App ___ (2015).
[2] *Id.*
[3] *Id.*

However, even though the court found that some software had been delivered, the court determined that under the *Catalina*[4] test ("incidental to service" test) the software was merely incidental to the vendor's "rendering of professional services." Specifically:

> [P]laintiff contracted with the businesses in order to receive services, and the tangible personal property was merely incidental to the provision of services. There is no indication that plaintiff could purchase the software or other tangible personal property independent of the services, and the services gave value to the software and other tangible personal property.[5]

In accordance with *Auto-Owners* and consistent with a series of cases[6] that require the Michigan Department of Treasury (the "Department") to give judicial decisions full retroactive effect – even in the presence of contrary guidance issued by the Department prior to the date of the decision – *Auto-Owners* will be applied to all open tax years.

Consequently, those portions of RAB 1999-5 that suggest that access to software over the internet without also the delivery of either "the code that enables the program" to operate or a "desk top client" are inconsistent with *Auto-Owners* and no longer represent the Department's policy. If only a portion of a software program is electronically delivered to a customer, the "incidental to service" test will be applied to determine whether the transaction constitutes the rendition of a nontaxable service rather than the sale of tangible personal property. However, if a software program is electronically downloaded in its entirety, it will be taxable.

II. Administrative Requirements for Taxpayers Seeking a Refund under *Auto-Owners*

A Taxpayer seeking a refund of taxes paid for a product falling within the *Auto-Owners* opinion should file a written refund request with the Department within the statute of limitations[7]. The request should include any necessary documentation to support the refund. If the refund is for a prior year, the taxpayer must include amended Annual Returns for the years involved with the refund request.

It should be noted that if the tax was paid to a vendor, the taxpayer must request a refund from the vendor. All refund requests filed pursuant to *Auto-Owners* and this Notice must be sent to the following addresses:

> Department of Treasury
> Attn: Technical Services
> P.O. Box 30698
> Lansing, MI 48909-8198

[4] *Catalina Marketing Sales Corp v Dep't of Treasury*, 470 Mich 13 (2004).
[5] ___ Mich App at _____.
[6] *Syntex Laboratories v Dep't of Treasury*, 233 Mich App 286 (1998); *Rayovac Corp v Dep't of Treasury*, 264 Mich App 441 (2004); *JW Hobbs v Dep't of Treasury*, 268 Mich App 38 (2005); *Int'l Home Foods Inc v Dep't of Treasury*, 477 Mich 983 (2007).
[7] MCL 205.27a.