STATE OF MICHIGAN

COURT OF APPEALS

HAMILTON'S HENRY THE VIII LOUNGE, Plaintiff-Appellant, v DEPARTMENT OF TREASURY, Defendant-Appellee.	UNPUBLISHED July 20, 2006 No. 267537 Court of Claims LC No. 04-000056-MT
HAMILTON'S BOGARTS, INC., Plaintiff-Appellant, v DEPARTMENT OF TREASURY, Defendant-Appellee.	No. 267538 Court of Claims LC No. 04-000057-MT
JO-BET, Plaintiff-Appellant, v DEPARTMENT OF TREASURY, Defendant-Appellee.	No. 267539 Court of Claims LC No. 04-000058-MT
GARTER BELT, INC., Plaintiff-Appellant,	

v

DEPARTMENT OF TREASURY,

Defendant-Appellee.

No. 267540
Court of Claims
LC No. 04-000059-MT

Before: Donofrio, P.J., and O'Connell and Servitto, JJ.

PER CURIAM.

Plaintiffs appeal as of right from the trial court's order granting defendant's motion for summary disposition. Because the General Sales Tax Act requires plaintiffs to pay sales tax on the entire amount charged for beverage sales, we affirm.

Plaintiffs are Michigan corporations (owned by one individual) that provide adult entertainment. In 2001, plaintiffs were audited by Steven Bielak, an auditing specialist with defendant, for the time period of January 1, 1998 through August 31, 2001. The audit revealed that plaintiffs categorized 50 percent of the amount charged to customers for beverages as "sales-entertainment" rather than as beverage sales, and did not pay sales taxes on this amount. It is undisputed that there are signs at the entrance and above the cash registers at each establishment that inform customers that "50% of the purchased drink price is for entertainment charges," and it is also clearly marked on each bill that 50 percent of the total cost was for entertainment and 50 percent was for drinks. According to Bielak, he found no justification for deducting 50 percent of plaintiffs' beverage sale proceeds as an entertainment fee, and he rejected plaintiffs' contention that the entertainment charge was a separately itemized fixed charge that was exempt from the sales tax. Plaintiffs argued that the entertainment charge constitutes an addition to the price of each drink, and disagreed with defendant's characterization of the practice as "deducting" 50 percent from their beverage sales. Nevertheless, at the conclusion of the audit, plaintiffs were notified that they each owed over $100,000 in additional sales taxes, interest, and penalties.

Plaintiffs paid at least the majority of the amount owed, then each filed suit to recover these amounts. The cases were consolidated pursuant to the parties' joint stipulation and defendant thereafter moved for summary disposition. The trial court granted defendant's motion for summary disposition under MCR 2.116(C)(10), concluding that the plain language of the General Sales Tax Act (GSTA), MCL 205.51 *et seq.,* required that sales tax be computed on the total gross proceeds for the total amount of tangible personal property sold and that entire amount of beverage sales were tangible personal property that must be taxed accordingly. The trial court also noted that the GSTA contained no provision allowing for the deduction of one half of all beverage sales as entertainment fees to be exempt from the sales tax.

On appeal, plaintiffs argue that the trial court failed to give proper deference to 1979 AC, R 205.116, one of defendant's administrative rules, which provides that the sales tax does not apply to separately itemized charges for entertainment or dancing. They further argue that the entertainment charge is not paid for tangible personal property, and therefore it is not included in the gross proceeds subject to the sales tax by the GSTA. We disagree.

A trial court's decision to grant or deny summary disposition in reviewed de novo. *Gen Motors Corp v Dep't of Treasury,* 466 Mich 231, 236; 644 NW2d 734 (2002). A motion for summary disposition brought under MCR 2.116(C)(10) tests the factual support for the plaintiff's claim. *Arias v Talon Development,* 239 Mich App 265, 266; 608 NW2d 484 (2000). In evaluating a motion brought under this subrule, the Court considers affidavits, pleadings, depositions, admissions, and other evidence submitted by the parties in the light most favorable to the party opposing the motion. *Spencer v Citizens Ins Co*, 239 Mich App 291, 299; 608 NW2d 113 (2000). When the proffered evidence fails to establish a genuine issue regarding any material fact, the moving party is entitled to judgment as a matter of law. *Id.* Questions of statutory interpretation are questions of law this court also reviews de novo. *Columbia Assoc, LP v Dep't of Treasury,* 250 Mich App 656, 665; 649 NW2d 760 (2002).

Because the relevant facts are not in dispute, the case turns on the proper interpretation of the GSTA. Payment of the sales tax is required under the GSTA:

> [T]here is levied upon and there shall be collected from all persons engaged in the business of making sales at retail, as defined in section 1 [1], an annual tax for the privilege of engaging in that business equal to 6% of the gross proceeds of the business, plus the penalty and interest if applicable. . .less deductions allowed by this act.[MCL 205.52].

During the years at issue in this case, MCL 205.51(1)(i) defined "gross proceeds" as:

> the amount received in money, credits, subsidies, property, or other money's worth in consideration of a sale at retail within this state, without a deduction for the cost of the property sold, the cost of material used, the cost of labor or service purchased, an amount paid for interest or a discount, a tax paid on cigarettes or tobacco products at the time of purchase, a tax paid on beer or liquor at the time of purchase, or other expenses.

Under MCL 205.51(1)(b), a "sale at retail" was defined, in relevant part, as "a transaction by which the ownership of tangible personal property is transferred for consideration, if the transfer is made in the ordinary course of the transferor's business and is made to the transferee for consumption or use, or for any purpose other than for resale, or for lease."

When interpreting a statute, the primary goal of the court is to ascertain and give effect to the intent of the Legislature. *By Lo Oil Co v Dep't of Treasury,* 267 Mich App 19, 49; 703 NW2d 822 (2005). In doing so, the Court should look first to the specific language of the statute, and, if the plain and ordinary meaning of the language is clear, judicial construction is neither necessary nor permitted. *Id.* If, on the other hand, reasonable minds could differ on the

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[1] PA 2004, No. 173, effective September 1, 2004 replaced the phrase "as defined in section 1" with "by which ownership of tangible personal property is transferred for consideration."

meaning of the statute, judicial construction is appropriate. *Id.* The Court should construe the statutory language reasonably, in light of the purpose of the act. *Id.* at 49-50. An administrative agency's interpretation of a statute within its responsibility should be given deference, but it cannot overcome the plain meaning of the statute. *Id.* at 50.

As a general rule, tax laws are construed against the government, while tax-exemption statutes are strictly construed in favor of the taxing unit. *DaimlerChrysler Corp v Dep't of Treasury,* 268 Mich App 528, 534; 708 NW2d 461 (2005). While ambiguities in the language of a tax statute should be resolved in the taxpayer's favor, if the dispute can be resolved by applying the ordinary and generally accepted meaning of the terms of the statute, the terms are not necessarily ambiguous. *Columbia Assoc, supra* at 687. Further, a taxpayer claiming an exemption from a tax bears the burden of proving the exemption, and only to the extent that there is a clear provision can any particular deduction be allowed. *ANR Pipeline Co v Dep't of Treasury,* 266 Mich App 190, 201; 699 NW2d 707 (2005); *Guardian Industries Corp v Dep't of Treasury,* 243 Mich App 244, 249; 621 NW2d 450 (2000).

Essentially, plaintiffs argue that the portion of the drink total designated as an entertainment charge does not fall within the statutory definition of gross proceeds because it is not a retail sale, i.e., the sale of tangible personal property, and therefore it is not subject to the sales tax. In support of their position, plaintiffs rely on 1979 AC, R 205.116(2), which states: "The [sales] tax applies to the cover or minimum charge and all other charges, except to those charges for entertainment and dancing, separately listed on the bill or collected as an admission fee or fixed charge."

Defendant argues that, to the extent that this rule creates an exemption from the sales tax that is not in the statute itself, it is invalid. We agree. This Court has held that liability for the payment of sales tax is dependent on the language of the GSTA and cannot be imposed or obviated by rules made by defendant. *Gainey Transportation Service, Inc v Dep't of Treasury,* 209 Mich App 504, 506-507; 531 NW2d 774 (1995). In other words, tax exemptions must rest on legislative action. *Id.* at 507. Interpretive rules are invalid if they conflict with the plain language of the statute itself or extend or modify the statute. *Guardian, supra* at 254. Further, it is clear that this Court is not bound by an agency's interpretation of a statute. *Id.*

Defendant further argues that plaintiffs cannot exclude the entertainment charge from their "gross proceeds" subject to the sales tax under MCL 205.52(1) because the statute does not contain a deduction for entertainment charges or fees. We agree that the plain language of the GSTA does not permit plaintiffs to exclude the entertainment charge from their gross proceeds. MCL 205.52 provides that the sales tax is collected on the gross proceeds of all persons engaged in the business of making sales at retail, less deductions allowed by the act. Plaintiffs admit that the primary purpose of their business is to sell alcoholic beverages. The sale of the beverages is a sale at retail because it involves the transfer of ownership of tangible personal property for consideration. Further, the definition of gross proceeds specifically disallows a deduction for the cost of materials, labor, service, or "other expenses." MCL 205.51(1)(i).

Plaintiffs cite *Natural Aggregates Corp v Dep't of Treasury,* 133 Mich App 441; 350 NW2d 272 (1984), for the proposition that a retail seller can simultaneously engage in a service business, the proceeds of which are not subject to the sales tax. See also MCL 205.52(2). Plaintiffs' reliance on *Natural Aggregates Corp* is misplaced, however, because, unlike in that

case, plaintiffs are not providing a service that constitutes a separate conceptual and temporal transaction from the retail sale, such as a delivery service. *Natural Aggregates, supra* at 446. Instead, the price of the entertainment is a component of the price of the product, and as such it is subject to the sales tax. See, e.g., *Earle Equip Co v Dep' t of Treasury,* 136 Mich App 536, 540-541; 358 NW2d 16 (1984).

Plaintiffs themselves acknowledge that the entertainment is offered to induce their customers to purchase drinks. In this respect, it is merely an expense that plaintiffs incur in the course of their business. Moreover, the transaction is principally a transfer of tangible personal property and creative accounting techniques cannot change that fact. The customer pays a set price for a drink, regardless of whether he wishes or intends to observe the entertainment. The sale of a drink is still a sale at retail and the total consideration for the sale is still the price paid by the customer to obtain the drink, even if the receipt indicates that 50 percent of the bill is actually an entertainment charge. Further, the entertainment offered by plaintiffs is not a "service" in the commonly understood sense of the word. The dancers pay the plaintiffs for the privilege to perform, and rely on tips from customers for compensation.

Because the statute is unambiguous and requires plaintiffs to pay the sales tax on the entire amount of beverage sales (including that portion labeled as entertainment charges), the trial court correctly granted defendant's motion for summary disposition.

Plaintiffs next argue that defendant is equitably estopped from collecting the sales tax in question because it had audited plaintiffs in the past and approved this accounting method. We disagree. "Equitable estoppel may arise where (1) a party, by representations, admissions, or silence intentionally or negligently induces another party to believe facts, (2) the other party justifiably relies and acts on that belief, and (3) the other party is prejudiced if the first party is allowed to deny the existence of those facts." *Conagra, Inc v Farmers State Bank,* 237 Mich App 109, 141; 602 NW2d 390 (1999). If the claim is based on silence or inaction, it must be shown that the silent party had a duty or obligation to speak or take action. *Id.*

There is no evidence in the record to support plaintiffs' claim that they were audited in the past. Although plaintiffs' CEO, John Hamilton, stated that plaintiffs were audited during the time in which they used the accounting practice at issue, the documents that plaintiffs rely on to support this assertion do not indicate that an audit was conducted, and consist only of tax bills, monthly statements, and letters relating to tax delinquency—all dated prior to 2001. Lacking evidence of a prior audit, plaintiff has failed to provide evidence that plaintiff had employed the accounting practice for some time or that defendant made any representation to plaintiffs on which to base their estoppel claim.

Plaintiffs' final argument on appeal is that the trial court erred in upholding the 10 percent negligence penalty they incurred. Again, we disagree. Under MCL 205.23(3), if defendant determines that a taxpayer has not satisfied a tax liability, and any part of the deficiency is due to negligence, a penalty of 10 percent of the total amount of the deficiency shall be added, which becomes due after notice and informal conference. However, if the taxpayer "demonstrates to the satisfaction of the department that the deficiency . . . was due to reasonable cause, the department shall waive the penalty." MCL 205.23(3).

Negligence is defined by defendant as a "lack of due care in failing to do what a reasonable and ordinarily prudent person would have done under the particular circumstances." 1979, AC, R 205.1012(1). Rule 205.1012(1) further provides that the "standard for determining negligence is whether the taxpayer exercised ordinary care and prudence in preparing and filing a return and paying the applicable tax in accordance with the statute."

Plaintiffs argue that they reasonably concluded from Rule 205.116(2) that a "fixed charge" for entertainment and dancing did not need to be included in their gross proceeds subject to the sales tax. Plaintiffs argue that their entertainment charge is "fixed" because the same percentage is used for all customers. Plaintiffs themselves note, however, that a "fixed fee" is defined as one "that will not vary according to the amount of work done or any other factor." Black's Law Dictionary (7th ed). Plaintiffs' entertainment charge, on the other hand, varies for each customer because it is based on the quantity and price of the drinks purchased. Plaintiffs' thus do not necessarily make a consistent, set amount for entertainment each day. Rather the income termed as entertainment is dependent upon and directly corresponds to the amount of drinks sold/business done. Therefore, it cannot reasonably be viewed as a "fixed charge."

Further, plaintiffs admit that they did not seek defendant's advice on this issue. In any event, it is clear that the statute does not make an exception for entertainment charges, as discussed above. Therefore, we agree that plaintiffs have not demonstrated " reasonable cause" for failing to include the amount charged as an entertainment fee in their gross proceeds, and therefore defendant was not required to waive the negligence penalty under MCL 205.23(3).

Affirmed.

/s/ Pat M. Donofrio
/s/ Peter D. O'Connell
/s/ Deborah A. Servitto