STATE OF MICHIGAN

COURT OF CLAIMS

TD AUTO FINANCE, L.L.C.,

Plaintiff,

v

NICK A. KHOURI, STATE OF MICHIGAN, and DEPARTMENT OF TREASURY,

Defendants.
_____/

OPINION AND ORDER

Case No. 17-000259-MT

Hon. Colleen A. O'Brien

Pending before the Court are: (1) defendants' August 1, 2018 motion for partial summary disposition; (2) defendants' August 17, 2018 motion for summary disposition; and (3) plaintiff's August 17, 2018 motion for partial summary disposition. For the reasons stated herein, defendants' August 17, 2018 motion for summary disposition is GRANTED, and the matter is dismissed. As a result, the remaining motions are DENIED as MOOT.

I. BACKGROUND

This matter arises out of plaintiff's request for a refund or deduction for sales tax paid on purportedly worthless installment contracts under the bad-debt statute, MCL 205.54i. According to the allegations in plaintiff's complaint, plaintiff is a financing company that financed the purchase of automobiles by consumers from automobile dealers in this state by way of retail installment contracts. Plaintiff's complaint alleges that some of the customers defaulted on the retail installment contracts, meaning that the full amount of the purchase price, as well as the

sales tax, was never paid to plaintiff. Plaintiff alleges that, after making reasonable attempts to collect the remaining unpaid balances, it determined that the defaulted-on accounts were worthless and uncollectible. Plaintiff alleges that it claimed these unpaid balances as bad debts pursuant to 26 USC 166 on its federal income tax returns.

On or about December 3, 2014, plaintiff filed a refund claim in the amount of $546,976.64 in connection with the defaulted-upon accounts under the bad-debt statute, MCL 205.54i. On June 19, 2017, defendant Department of Treasury ("the Department") issued a partial refund or deduction in the amount of $77,324.64, but denied the remainder of the request.[1] The denial is the subject of this instant action. In short, plaintiff contends that it satisfied the conditions of the bad-debt statute, such that it is entitled to a refund of the entire amount claimed in its December 3, 2014 request.

II. DEFENDANTS' AUGUST 17, 2018 MOTION FOR SUMMARY DISPOSITION

On August 17, 2018, defendants moved this Court for summary disposition, contending that plaintiff failed to support its refund claim with the level of documentation that the Department, under the bad-debt statute, has the discretion to request. In particular, defendants requested accounting records demonstrating that the accounts at the heart of the bad-debt deduction were in fact written off as worthless or uncollectible on plaintiff's internal accounting records. Defendants note that it requested such information throughout the pendency of litigation, but plaintiff declined to provide the same. By and large, plaintiff does not dispute that it failed to provide the records the Department requested. Instead, plaintiff provided what it

[1] The Department now contends that it "mistakenly" refunded these amounts.

contends are summaries—prepared by counsel—of the records sought. Travis Gilbert, the Vice President and Head of State and Local Tax for plaintiff's parent company, TD Bank NA, testified at deposition that the summaries were prepared from plaintiff's own records.

A. THE BAD-DEBT DEDUCTION

In general, the bad-debt deduction is a deduction from a taxpayer's gross proceeds under the General Sales Tax Act (GSTA). MCL 205.54i; *Ally Fin, Inc v State Treasurer*, __ Mich __; __ NW2d __ (2018) (Docket Nos. 154668; 154668; 154670); slip op at 8. In order to claim the deduction, there must be, at a minimum, a "bad debt." MCL 205.54i(1)(a) defines "bad debt," in pertinent part, as "any portion of a debt that is related to a sale at retail taxable under this act for which gross proceeds are not otherwise deductible or excludable and that is eligible to be claimed, or could be eligible to be claimed if the taxpayer kept accounts on an accrual basis, as a deduction pursuant to section 166 of the internal revenue code, 26 USC 166." The statute declares that, in order to be eligible for the deduction, the debt must be that which is "charged off as uncollectible on the books and records of the taxpayer at the time the debt becomes worthless . . . ." MCL 205.54i(2).

Because taxation is the rule and refunds or deductions are the exception, the taxpayer bears the burden of demonstrating entitlement to a refund or deduction. *Andrie Inc v Dep't of Treasury*, 496 Mich 161, 171; 853 NW2d 310 (2014). Moreover, MCL 205.54i(4) expressly declares that "Any claim for a bad debt deduction under this section *shall be supported by that evidence required by the department*." (Emphasis added). In *Ally Fin*, __ Mich at __; slip op at 18, our Supreme Court interpreted MCL 205.54i(4) as giving the Department discretion "to determine the evidence required to support a party's claim for a deduction or refund." The exercise of that discretion must be upheld if it is supported by a rational basis. *Id*. In that case,

the evidence required by the Department was an "RD-108" form expressly indicating that sales tax had been paid. *Id*. at 19. The Department in *Ally Fin* determined that the plaintiffs' own internal records accounting for tax payments did not show that the taxes were actually remitted; hence, the Department's decision to demand the RD-108 forms in order to demonstrate that the tax was paid was not an abuse of discretion. *Id*. at 19.[2]

Returning to the instant case, the issue raised by defendants concerns MCL 205.54i(4) and whether plaintiff has supported its claims with "that evidence required by the department." The Department demanded all or a portion of plaintiff's own accounting records showing that the accounts at issue were charged off as uncollectible by plaintiff. Plaintiff has, by all accounts, not produced its own internal accounting records. In accordance with *Ally Fin*, the issue in this case is whether the Department was within its discretion to demand plaintiff's own accounting records to demonstrate that the accounts had, in fact, been written off as uncollectible. Resolution of this issue requires an examination of the records produced by plaintiff.

B. THE INCOME TAX RETURNS DO NOT PROVIDE THE REQUISITE SUPPORT

The first set of documents discussed in defendants' motion are income tax returns filed by TD Bank NA and TD Auto for the 2011-2013 tax years. The returns list a number of categories pertinent to the return, including a line for "bad debts." The returns indicate that plaintiff and its parent company claimed bad debts on their federal income tax returns from 2011-2013. However, the documents do nothing more than that. They do not include a

[2] Moreover, the Court noted that the plaintiffs in that case *could* have obtained the refunds they sought because they could have, at what was described as a "reasonable cost," obtained the RD-108 forms from the Secretary of State. *Ally Fin*, __ Mich at __; slip op at 19 n 41.

breakdown of the source of the bad debts (e.g., whether the bad debts originated from retail installment contracts written off as uncollectible), nor do they provide any information on *where* the contracts originated from. This is significant, because plaintiff transacts business in states other than Michigan, such that the federal income tax returns conceivably included bad debts incurred in other states as well. Nor do the returns shed any light on whether the retail installment contracts that are the subject of plaintiff's refund claim in the instant case were even included in the broad category of "bad debts" claimed on plaintiff's and plaintiff's parent company's federal income tax returns. In short, the federal income tax returns do not offer any evidence on the matter of whether the accounts at issue in this bad-debt deduction claim were in fact written off as uncollectible by plaintiff.

C. THE SPREADSHEETS PREPARED BY PLAINTIFF

The next set of records—and the primary point of contention in this case—are the spreadsheets produced by plaintiff's counsel during discovery. In evaluating these spreadsheets, it must be noted that there is no dispute that the spreadsheets are not copies of accounting records kept by plaintiff; instead, they are purportedly summaries of information derived from plaintiff's accounting records and prepared by plaintiff's counsel. This Court's review of the spreadsheet reveals that the documents generally lists names and account numbers of debtors, and they include a column indicating the vehicle model/make, vehicle model year, VIN, and contract date. And, of particular significance to the instant case, the spreadsheets have a column for each account labeled "Charge Off Date." For each account, a separate page contains more details about the customer and the dealer that sold the automobile that was the subject of the retail-installment contract. Further, the spreadsheets purport to list information regarding the applicable sales tax rate, the taxable sales price of the automobile, the applicable sales tax, the

total amount financed, the amount of plaintiff's loss, and the refund or deduction amount claimed for each account.

D. THE DEPARTMENT DID NOT ABUSE ITS DISCRETION BY REQUESTING ADDITIONAL RECORDS, AND THE SPREADSHEETS DO NOT SATISFY PLAINTIFF'S BURDEN

The Court agrees with defendants' contention that the spreadsheets do not satisfy plaintiff's statutory obligation of producing those records requested by the Department under the bad-debt statute. Again, the bad-debt statute grants the Department discretion to demand that a bad-debt deduction claim "be supported by that evidence required by the department." MCL 205.54i(4); *Ally Fin*, __ Mich at __; slip op at 17-18. As stated in *Ally Fin*, __ Mich at __; slip op at 18, "[w]hen an agency is granted discretion by a statute, the agency's exercise of that discretion will be upheld if supported by a rational basis." Here, a rational basis exists to support the Department's decision to demand some form of plaintiff's own accounting records, rather than the spreadsheets produced here. To that end, the spreadsheets, despite containing a purported "charge-off" date, are not records demonstrating that plaintiff actually wrote the accounts off as worthless or uncollectible on its own accounting records. As defendants note, plaintiff's accounting records would be the primary and best source of evidence to demonstrate that plaintiff had in fact charged off the accounts as uncollectible. And plaintiff has not, despite several requests, produced the records demanded by the Department. The spreadsheets are problematic as well because they appear to contain accounts that were either determined to be paid in full, were the subject of satisfied civil judgments, or for which plaintiff may have sold the account in question to a third party. The Court agrees with the Department's contention that a resort to plaintiff's own accounting records could have resolved such issues. In theory, the records should not have been difficult to obtain, because according to Gilbert's deposition

testimony, the accounting records from which the spreadsheets were drawn were in plaintiff's possession and plaintiff's accounting department purportedly utilized the records when it prepared the spreadsheet compilations. Thus, the Department simply asked for records which plaintiff should have been able to produce. In light of the apparent problems with the spreadsheets, and in light of the fact that plaintiff possessed—and used the same to prepare the spreadsheets—the records the Department sought, the Department did not abuse its discretion. See *Ally Fin*, __ Mich at __; slip op at 17-19.

In resolving this issue, the Court analogizes the instant case to *Ally Fin*. As noted, in *Ally Fin*, the Department requested the plaintiffs produce RD-108 forms in order to show that sales tax was remitted on the automobiles that were the subject of the bad-debt accounts. *Id*. at 18-19. Although the plaintiffs in that case provided "their own internal records accounting for the payments," those records did *not* show that tax payments were actually made or that the amount of taxes paid. *Id*. The RD-108 forms would have demonstrated that the tax was indeed paid, and those forms were available to the plaintiff via requests made to the Secretary of State's office. *Id*. Returning to the instant case, plaintiff declined, on multiple occasions, to provide accounting records to show that plaintiff in fact charged off the accounts at issue as uncollectible. Plaintiff provided federal income tax returns showing a total amount written off as "bad debts," but there is no indication whatsoever that any of the accounts at issue in this case were among the "bad debts." Moreover, plaintiff's spreadsheets, although they include a column indicating a "charge off" date, do not demonstrate that the accounts were actually written off by plaintiff. And as noted above, the spreadsheets appeared to contain accounts that were ineligible to be claimed as bad debts. Plaintiff, according to Gilbert, created the summaries by consulting its own records, but plaintiff failed or declined to produce those records. Just like in *Ally Fin*, where the records

produced by plaintiff did not provide evidence of that which they were submitted to demonstrate, i.e., that the accounts were written off and qualified as "bad debts," the Department's decision to demand records that were, in theory, accessible to plaintiff was not an abuse of discretion. See *Ally Fin*, __ Mich at __; slip op at 18-19.

In responding to the defendants' arguments, plaintiff contends that a question of fact which precludes summary disposition. Plaintiff acknowledges that Treasury has identified some potential issues regarding whether all of the accounts listed in the spreadsheets are eligible to be claimed under the bad-debt deduction statute. According to plaintiff, all defendants have done is identify conflicting documentary evidence, which, according to plaintiff, represents a reason to deny summary disposition at this time. Plaintiff is correct that generally, conflicting documentary evidence requires a court to deny summary disposition. See, generally, *Pioneer State Mut Ins Co v Dells*, 301 Mich App 368, 377; 836 NW2d 257 (2013). However, plaintiff's argument fails to address the pertinent issue. The issue here in this case, as noted in *Ally Fin*, concerns the Department's discretion to demand certain evidence under MCL 205.54(4). The Department has exercised that discretion by demanding that plaintiff produce its own internal accounting records or documents. The Department did so, it appears at least in part, *because* there was conflicting documentary evidence regarding the accounts at the heart of plaintiff's bad-debt deduction claim. In accordance with the Supreme Court's decision in *Ally Fin*, this Court is asked to determine whether the Department abused its discretion in requesting the documents at issue, not whether the documentary evidence that led to the request in the first place creates a genuine issue of material fact.

In short, the Department properly exercised its discretion in requesting plaintiff's own internal accounting records under the circumstances present in this case. Because plaintiff,

despite numerous request, failed to produce "that evidence required by the department," defendants are entitled to summary disposition. See *Ally Fin*, __ Mich at __; slip op at 17-19.[3]

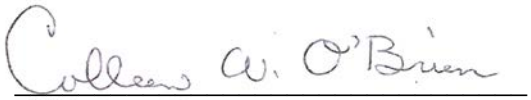
III. CONCLUSION

IT IS HEREBY ORDERED that defendants' August 17, 2018 motion for summary disposition is GRANTED.

IT IS HEREBY FURTHER ORDERED that defendants' August 1, 2018 motion for partial summary disposition, as well as plaintiff's August 17, 2018 motion for partial summary disposition, are DENIED as MOOT.

This order resolves the last pending claim and closes the case.

Dated: October 30, 2018



Colleen A. O'Brien, Judge
Court of Claims

[3] Defendants' briefing addresses other categories of records submitted in this case, such as sample RD-108 forms, written election agreements, and retail installment contracts. These documents—about which plaintiff has not presented an argument—do not address the issue of whether plaintiff in fact wrote the accounts off as uncollectible on its own books and records.