

Resources

Michigan Clarifies Taxation of Online Software Services and Provides Refund Opportunities

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The application of the Michigan sales and use taxes to payments for remote access to software programs has been a controversial subject for many years and litigated by several taxpayers. The emergence of “cloud computing” arrangements that enable a customer to use the Internet to access software or receive services has raised issues about how such transactions should be taxed. Now, a taxpayer-favorable decision by the Michigan Court of Appeals in the *Auto-Owners Insurance Company* case has caused the Michigan Department of Treasury (the “Department”) to revise its policy with respect to such payments.

On January 6, 2016, the Department published a Notice to Taxpayers Regarding *Auto-Owners Insurance Company v. Department of Treasury* (the “Notice”, available [here](#)). The Notice addresses the recent *Auto-Owners* ruling in which the Court agreed with the taxpayer that its payments for the use of certain prewritten computer software programs were exempt from Michigan’s use tax. *Auto-Owners Insurance Company v. Department of Treasury*, __ Mich. App. __ (2015). The Court ruled that prewritten computer software that the taxpayer accessed online without downloading was not subject to use tax because the software was not delivered to the taxpayer. Further, the Court applied the *Catalina* “incidental to service” test in holding that certain software that the taxpayer partially downloaded was not subject to use tax because the taxpayer’s “real object” was to purchase a service, not tangible personal property. See *Catalina Marketing Sales Corp. v. Department of Treasury*, 470 Mich. 13 (2004).

As a result of the *Auto-Owners* case (and other similar taxpayer-favorable cases), the Department announced in the Notice that it will apply the Court of Appeals’ rulings both prospectively and retroactively to all tax periods open under the statute of limitations. The Notice also specifies procedures required for taxpayers to seek refunds of tax for software products of the type at issue in *Auto-Owners*. A wide range of software programs were at issue, including not only insurance industry specific applications but also more generally used applications such as online research services, communication services, payment processing services, equipment maintenance and customer support programs.

A taxpayer who paid use tax directly to the Department can file a written refund request to the Department and should include amended use tax returns for any prior tax periods. A taxpayer who paid sales tax to a software vendor must request a refund from the vendor (who in turn must seek the tax refund from the Department). Generally speaking, refund claims must be filed within four years of the date the original tax return was filed.

If you would like to discuss the application of the Notice to your situation, or need assistance in filing refund claims, please contact Steve Grob (sgrob@dykema.com), Mary Hennessey (mhennessey@dykema.com), or your Dykema relationship attorney.

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