

SC91784

IN THE SUPREME COURT OF MISSOURI

AQUILA FOREIGN QUALIFICATIONS CORPORATION,

Respondent (Petitioner below),

vs.

DIRECTOR OF REVENUE,

Appellant (Respondent below).

From the Administrative Hearing Commission
The Honorable Karen A. Winn, Commissioner

BRIEF OF APPELLANT

CHRIS KOSTER
Attorney General

JEREMIAH J. MORGAN
Mo. Bar No. 50387
Deputy Solicitor General
Supreme Court Building
P.O. Box 899
Jefferson City, MO 65102-0899
(573) 751-1800
(573) 751-0774 (Facsimile)
Jeremiah.Morgan@ago.mo.gov

ATTORNEYS FOR APPELLANT
DIRECTOR OF REVENUE

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JURISDICTIONAL STATEMENT

The issues before the Court in this matter involve the construction of § 144.054.2, RSMo (2010 Cum. Supp.),^{1/} a revenue law of the State of Missouri. Therefore, this Court has exclusive jurisdiction over this matter pursuant to Article V, § 3 of the Missouri Constitution.

^{1/} All references to the Missouri Revised Statutes are to the 2010 Cumulative Supplement unless otherwise specified.

STATEMENT OF FACTS

Aquila is a large electric utility company selling electricity to residential and commercial customers in Missouri, including Casey's General Store ("Casey's"). (LF 12; Appellant's Appdx. A1-A2). At the request of Casey's, Aquila challenged the Director of Revenue's decision to deny a refund of less than \$130 on sales taxes paid for electricity at two of Casey's retail gas station convenience stores, one located in Grain Valley, and the other in Greenwood, Missouri. (LF 12; Appdx. A2).

Aquila claims, on behalf of Casey's, that a portion of the electricity at the two retail gas station convenience stores is exempt from state sales tax under § 144.054.2, because the electricity is supposedly used in "manufacturing, processing, compounding, mining, or producing" a product under § 144.054.2. (LF 13-16).

A. Casey's Represents Itself as a Convenience Store, Not a Manufacturer or Processor.

Prior to Aquila seeking this refund of sales tax, Casey's did not claim to be a manufacturer when registering with the local taxing jurisdictions where the stores at issue are located. (LF 169). Instead, the Grain Valley and Greenwood Casey's stores represented that they were retail gas station convenience stores in their government filings with Jackson County and the cities of Grain Valley and Greenwood. (*Id.*). Casey's described its activities as "convenience store,

retail sales, gas, grocery, prepared foods” in the Business Information Sheet filed with the Jackson County Assessment Department. (*Id.*).

In the Business License Application filed with the City of Grain Valley, Casey’s used the NAICS code for gasoline stations with convenience stores and not the NAICS code for food manufacturers. (*Id.*). Likewise, in the Business License Application filed with the City of Greenwood, Casey’s described its activities as “convenience store, grocery items, bakery, [and] fuel.” (*Id.*). The Grain Valley and Greenwood stores are also not in areas zoned as light or heavy industrial districts; instead, they are located in areas zoned as central or general business districts. (*Id.*).

Casey’s similarly holds itself out as an operator of retail gas station convenience stores in its filings with the Securities and Exchange Commission (“SEC”). (*Id.*). All of Casey’s stores offer gasoline for sale on a self-serve basis and carry a broad selection of food (including freshly prepared foods in snack centers), beverages, tobacco products, health and beauty aids, automotive products, and other non-food items. (*Id.*). According to its 10-K filing with the SEC, “[m]anagement believes its stores located in small towns compete principally with other local grocery and convenience stores; similar retail outlets; and, to a lesser extent, prepared food outlets, restaurants, and expanded gasoline stations offering a more limited selection of grocery and food items for sale.” (LF 192-93).

Missing in the various descriptions provided by Casey's to governmental entities is any comparison to a manufacturer or processor. Its comparisons are all with retail grocery stores or restaurants. Additionally, in its own descriptions Casey's does not use industrial-type terms such as "manufacturing, processing, compounding, mining, or producing," but instead Casey's uses terms and phrases such as "freshly prepared foods" and "prepared foods." (LF 192 (emphasis added)).

B. Convenience Stores Like Casey's are Similar to Take-out Restaurants and Typically Heat Up Frozen Food.

Like most gas stations with a convenience store, Casey's has gas pumps under a canopy in the front of each store, aisles of merchandise of food and other items similar to a grocery store, a front check-out area with cigarettes for sale, refrigerators displaying items for sale, and a kitchen that is located behind the food area. (LF 191). There is a strong similarity between Casey's activities and those of a take-out restaurant: the bottom of the menu board is visibly hanging over a counter in front of the kitchen where customers can place their orders (the limited amount of food visible in the food warmers demonstrate that not every item on the menu is always on-hand for a customer to pick up). (LF 170). There is also typically no seating in the food area for customers. (LF 191).

The Grain Valley and Greenwood Casey's stores sell a variety of items to retail customers that are prepared in the stores: ice, meals and prepared food such as pizza, sandwiches, and pastries. (LF 170). They also serve hot and cold

drinks. (*Id.*). The food preparation area is described by Casey's as a snack center or as Casey's Kitchen. (*Id.*).

The amount of preparation required prior to selling food items to customers varies and involves activities such as heating, cooling, thawing, frying, baking, mixing, cutting, preparing, or cooking of food. (LF 171). For example, brownies are prepared for selling to customers by merely removing the pre-formed and pre-cooked brownies from the freezer and thawing; at times, icing may be added to some brownies. (*Id.*). On the other end of the spectrum are cake donuts: the donuts are prepared at the stores by mixing pre-processed donut flour ("Casey's cake donut flour") with water to form dough that is fried; icing and toppings are applied after cooling. (*Id.*). Most items involve an amount of preparation between the above two extremes.

The most common type of food preparation at a Casey's convenience store is taking pre-processed food (often frozen and pre-cooked) and heating it in an oven. (*Id.*). For example, breakfast sandwiches, hash browns, biscuits & gravy, long johns, chicken tender sandwiches, sausage sandwiches, hamburgers, cheeseburgers, potato cheese bites, chicken pot pie bites, popcorn chicken, mini pizza bites, potato wedges, and BBQ sandwiches all involve frozen and pre-cooked items being heated in an oven. (*Id.*).

C. The Commission’s Decision Creates a New and Broad Definition of “Processing.”

Before engaging in its analysis, the Administrative Hearing Commission (“Commission”) set out its “Findings of Fact.” (LF 601-17; Appdx. A2-A18). The findings by the Commission use typical language to describe the process of preparing food at Casey’s, including such language as “prepared by mixing”; “gently rolled”; “hand rolled”; “sliced”; “ladled”; and “freshly brewed.” (LF 604-08, 615; Appdx. A5-A7, A16).

In its analysis, the Commission found on the one hand that “[a]ll of these statutes (including § 144.054) provide . . . favored tax treatment for those who manufacture products” and “Casey’s is primarily a retailer that sells prepared food, and it is not a ‘manufacturer.’” (LF 624; Appdx. A25 (emphasis added)). In contrast, the Commission later concluded that stores like Casey’s that “transform materials such as frozen food into ready-to-eat food items” satisfy the manufacturing exemption. (LF 621, 624, 628; Appdx. A22, A25, A29). The difference, according to the Commission, is the use of the term “processing” in the list of “manufacturing, processing, compounding, mining, or producing” covered under § 144.054.2. (LF 624; Appdx. A25).

Although the Commission noted that this Court has found that “the meaning of the term “processing” is ordinarily included within the meaning of the more general and inclusive term “manufacturing,”” (LF 624; Appdx. A25 (quoting *Mid-America Dairymen, Inc. v. Dir. of Revenue*, 924 S.W.2d 280, 282

(Mo. banc 1996)), it nevertheless decided that “processing” is now different under § 144.054.2. And in the process, the Commission decided not to follow this Court’s decision in *Brinker Mo., Inc. v. Dir. of Revenue*, 319 S.W.3d 433 (Mo. banc 2010).

POINT RELIED ON

The Commission Erred in Refunding Sales Tax Paid by Casey's on its Purchases of Electricity, In That a Retail Gas Station and Convenience Store Does Not Qualify for a Tax Exemption Under § 144.054.2, Because Casey's Food Preparation is Not "Processing" at a "Production Facility."

Brinker Mo., Inc. v. Dir. of Revenue,

319 S.W.3d 433 (Mo. banc 2010)

Branson Properties USA, L.P. v. Dir. of Revenue,

110 S.W.3d 824 (Mo. banc 2003)

Utility Serv. Co., Inc. v. Dep't of Labor and Indus. Relations,

331 S.W.3d 654 (Mo. banc 2011)

Reichert v. Bd. of Educ. of City of St. Louis,

217 S.W.3d 301 (Mo. banc 2007)

§ 144.054.2

SUMMARY OF THE ARGUMENT

Dressed up in a seemingly innocuous refund claim of less than \$130, Aquila argues on behalf of Casey's that the preparation of food at a convenience store is "processing" of a product under § 144.054.2. This is a wolf in sheep's clothing, to be sure. The impact of such a claim, in fact, would be devastating to Missouri sales tax. And the interpretation of § 144.054.2, advanced by Aquila and adopted by the Commission, is inconsistent with the plain language of the statute, the context and statutory structure, and department regulations. The interpretation would also produce absurd and illogical results.

This Court in *Brinker Mo., Inc. v. Dir. of Revenue*, 319 S.W.3d 433, 434 (Mo. banc 2010) established that restaurants do not "manufacture," but instead "prepare" meals – a common sense and appropriately narrow construction of a sales tax exemption. As such, restaurants are not entitled to manufacturing exemptions. Undeterred by this Court's decision in *Brinker*, Aquila is now attempting to fit a convenience store that prepares food (typically by heating up frozen food) under the cloak of yet another manufacturing exemption. This loose, if not statutorily untethered interpretation, would entirely undo the decision in *Brinker*, as § 144.054.2 also exempts "machinery, equipment, and materials" for manufacturing.

Contrary to the Commission's decision in this case, § 144.054.2 does not apply to restaurants or convenience stores that "prepare food" but instead to production facilities that engage in "manufacturing, processing, compounding,

mining, or producing” – all terms that denote large scale industrial-type actions. Indeed, the definition of “processing” includes the terms “production facility.” See *Hudson Foods, Inc. v. Dir. of Revenue*, 924 S.W.2d 277 (Mo. banc 1996) (referring to large industrial “plants” as “processing facilities”).

Additionally, the context and statutory structure undermine any expansion of a manufacturing exemption to restaurants or convenience stores that prepare food. The legislature specifically provided for sales taxes at places in which “meals or drinks are regularly served to the public.” § 144.020.1(6). But the legislature did not provide a corresponding exemption from sales taxes at such locations. And if the manufacturing exemption in § 144.054.2 did apply to all restaurants, convenience stores, and other places in which meals or drinks are regularly served to the public, then the list of exempt entities, and the corresponding impact on state sales tax, would be devastating. The Commission (until this case), as well as courts throughout the country, have rejected such an interpretation. This Court should likewise reject the dramatic expansion of manufacturing exemptions for restaurants and convenience stores, and thereby reverse the Commission.

ARGUMENT

Standard of Review

The only issues in this case are legal issues, and they involve the interpretation of a revenue law – § 144.054.2. This Court reviews the Commission’s interpretation of revenue laws *de novo*. *Brinker Mo., Inc. v. Dir. of Revenue*, 319 S.W.3d 433, 436 (Mo. banc 2010) (“Statutory interpretation is an issue of law that this Court reviews *de novo*.”); *Finnegan v. Old Republic Title Co. of St. Louis, Inc.*, 246 S.W.3d 928, 930 (Mo. banc 2008).

Section 144.054 is not just any revenue law; instead, it provides for sales and use tax exemptions. *See* § 144.054 (“Additional sales tax exemptions for various industries and political subdivisions.”). This distinction is especially important because tax exemptions are “strictly construed against the taxpayer.” *Branson Properties USA, L.P. v. Dir. of Revenue*, 110 S.W.3d 824, 825 (Mo. banc 2003); *Dir. of Revenue v. Armco, Inc.*, 787 S.W.2d 722, 724 (Mo. banc 1990) (noting that “strict construction is mandated for statutes establishing conditions for claiming an exemption”) (citing *Mo. Pub. Serv. Comm’n v. Dir. of Revenue*, 733 S.W.2d 448, 449 (Mo. banc 1987)). Indeed, an exemption is allowed “only upon clear and unequivocal proof, and doubts are resolved against the party claiming it.” *Id.* As such, the burden is on the taxpayer claiming the exemption “to show that it fits the statutory language exactly.” *Cook Tractor Co., Inc. v. Dir. of Revenue*, 187 S.W.3d 870, 872 (Mo. banc 2006).

In this case, Aquila cannot satisfy the burden to show that the ultimate taxpayer – Casey’s – fits the statutory exemption at all, much less exactly. Accordingly, the Commission’s decision to refund taxes under the exemption in § 144.054.2 should be reversed and judgment entered in favor of the Director of Revenue.

The Commission Erred in Refunding Sales Tax Paid by Casey’s on its Purchases of Electricity, In That a Retail Gas Station and Convenience Store Does Not Qualify for a Tax Exemption Under § 144.054.2, Because Casey’s Food Preparation is Not “Processing” at a “Production Facility.”

As with any statutory provision, “the primary rule of statutory interpretation is to give effect to legislative intent as reflected in the plain language of the statute.” *Akins v. Dir. of Revenue*, 303 S.W.3d 563, 565 (Mo. banc 2010) (citing *State ex rel. White Family Partnership v. Roldan*, 271 S.W.3d 569, 572 (Mo. banc 2008)). Statutory language is given its “plain and ordinary meaning.” *United Pharm. Co. of Mo., Inc. v. Mo. Bd. of Pharm.*, 208 S.W.3d 907, 910 (Mo. banc 2006).

Furthermore, “[n]o portion of a statute is read in isolation, but rather is read in context to the entire statute, harmonizing all provisions.” *Utility Serv. Co., Inc. v. Dep’t of Labor and Indus. Relations*, 331 S.W.3d 654, 658 (Mo. banc 2011). Indeed, “[a]scertaining and implementing the policy of the General Assembly requires the court to harmonize all provisions of the statute.” *20th &*

Main Redevelopment Partnership v. Kelley, 774 S.W.2d 139, 141 (Mo. banc 1989). It is likewise essential that the “[c]onstruction of statutes should avoid unreasonable or absurd results.” *Reichert v. Bd. of Educ. of City of St. Louis*, 217 S.W.3d 301, 305 (Mo. banc 2007).

The Director interpreted § 144.054.2 consistent with its plain and ordinary meaning, the statutory context of the sales and use tax exemption, and in a way that avoids truly unreasonable and absurd results. The Commission, however, did not. And its decision violates each of these principles of statutory construction, not to mention the narrow or strict construction that must be applied to sales tax exemptions.

A. The Plain and Ordinary Meaning of “Processing” Does Not Include Simply Heating Up Frozen Foods at Casey’s.

The statutory provision at issue – § 144.054.2 – provides in relevant part as follows:

In addition to all other exemptions granted under this chapter, there is hereby specifically exempted . . . electrical energy and gas, whether natural, artificial, or propane, water, coal, and energy sources, chemicals, machinery, equipment, and materials used or consumed in the manufacturing, processing, compounding, mining, or producing of any product . . .

Id. (emphasis added). Although Aquila argued to the Commission that the two Casey’s convenience stores in this case engage in “manufacturing,” “processing,” and “producing” a product that would qualify for the manufacturing exemption in § 144.054.2,^{2/} the Commission only considered the “processing” claim in its decision.

According to the Commission, Casey’s “acts constitute ‘processing’” because they “transform materials such as frozen food into ready-to-eat food items.” (Appdx. A29). However, this is not “processing” at a “production facility” under § 144.054.2, any more than preparing food at a restaurant is “manufacturing or producing food.” *Brinker*, 319 S.W.3d at 433. The plain language, if it really is to be narrowly construed as required by law, cannot be interpreted so broadly as to turn the term “processing” into a generic term that would cover virtually any activity by any business with any product.

To begin the analysis, we first turn to the statutory definition. The statute provides that “processing” is:

^{2/} Aquila did not, however, contend that Casey’s activities were “compounding” or “mining.” Yet, under Aquila’s (and the Commission’s) broad view of the statutory exemption in § 144.054.2, Casey’s activities are as equally “compounding” (*e.g.* making a sandwich) or “mining” (*e.g.* making ice) as they are “processing.”

[A]ny mode of treatment, act, or series of acts performed upon materials to transform or reduce them to a different state or thing, including treatment necessary to maintain or preserve such processing by the producer at the production facility

§ 144.054.1(1). This is the exact same definition used by the legislature in § 144.030.2(12), and under which restaurants have been rejected as manufacturers. *See Brinker*, 319 S.W.3d at 433. In addition, it is a definition that has been considered by this Court repeatedly. *See Mid-America Dairymen, Inc. v. Dir. of Revenue*, 924 S.W.2d 280, 283 (Mo. banc 1996); *Hudson Foods, Inc. v. Dir. of Revenue*, 924 S.W.2d 277, 278, fn. 1 (Mo. banc 1996); *State ex rel. Union Elec. Co. v. Goldberg*, 578 S.W.2d 921, 924 (Mo. banc 1979).

In *Hudson Foods* and *Mid-America Dairymen*, this Court found that “there is little to no difference between the terms ‘processing’ and ‘manufacturing.’” *Hudson Foods*, 924 S.W.2d at 278 n.1. In short, “the meaning of the term ‘processing’ is ordinarily ‘included within the meaning of the more general and inclusive term “manufacturing.””” *Mid-America Dairymen*, 924 S.W.2d at 283 (quoting *State ex rel. Union Elec. Co.*, 578 S.W.2d at 924). This definition of “processing,” as ordinarily included within the meaning of the term “manufacturing,” was well established when the legislature adopted the same definition of “processing” in § 144.054. Even the Commission in this case, contrary to its ultimate conclusion, considered § 144.054 a manufacturing

exemption. See Appdx. A22 (“All of these statutes provide, in one form or another, favored tax treatment for those who manufacture products in this state.”).

Both *Hudson Foods* and *Mid-America Dairymen* involved classic industrial-type processing. *Hudson Foods*, for example, involved mass poultry processing, see *id.* at 277 (noting the birds were “stunned, killed, bled, scalded, defeathered, and eviscerated”), while *Mid-America Dairymen* concerned large dairy processing operations, see *id.* at 281 (describing the “processing of raw milk into various dairy and related food products”). Neither case involved the preparation of food for retail sale such as heating up frozen food, but instead was what a lay person would actually consider “processing.” This type of large-scale industrial-type “processing” examined in *Hudson Foods* and *Mid-America Dairymen* is also consistent with dictionary definitions of the term. See *State ex rel. Burns v. Whittington*, 219 S.W.3d 224, 225 (Mo. banc 2007).

The dictionary provides the following relevant definitions for the term “processing:”

Process \ processed \ processing \ processes – 2a(1): to prepare for market, manufacture, or other commercial use by subjecting to some process <~ing cattle by slaughtering them> <~ed the milk by pasteurizing it> <~ing grain by milling> <~ing cotton by spinning> **(2)** to make usable by

special treatment <~ing rancid butter> <~ing waste material> <~ed the water to remove impurities>

Webster's Third New International Dictionary 1808 (1993). Even the examples given in the dictionary, such as processing cattle by slaughtering them or processing grain by milling, suggest large-scale industrial-type processing. This type of narrow or strict reading is consistent with how tax exemptions are to be applied, not an interpretation that would include heating up frozen food at a corner convenience store.

The legislature certainly could have used terms in § 144.054.2 consistent with retail food sales or restaurants or convenience stores – like “cooking,” “cutting,” or “frying” – but instead it selected industrial processing type terms such as “manufacturing, processing, compounding, mining, or producing.” § 144.054.2. If the legislature intended to apply the manufacturing exemption under § 144.054.2 to retail gas station convenience stores, it would have selected more appropriate language to do so. Thus, the plain and ordinary meaning of “processing,” as narrowly or strictly construed, should apply.

B. The Statutory Structure and Context Support the Plain Language's Narrow Application to Large-Scale Industrial-Type “Processing” at a “Production Facility.”

Not only does the plain language of the statute support the conclusion that Casey's is not “processing” products under § 144.054.2, but the statutory

structure and context also supports that same common sense conclusion. *See State ex rel. Burns*, 219 S.W.3d at 225. An important rule of statutory construction is that the provisions of a statute are “not read in isolation but construed together, and if reasonably possible, the provisions will be harmonized with each other.” *Bachtel v. Miller Co. Nursing Home Dist.*, 110 S.W.3d 799, 801 (Mo. banc 2003); *Mid-America Dairymen*, 924 S.W.2d at 283 (interpreting provisions in the same tax exemption statute “hand-in-hand”). Here, the statutory structure and context support the plain and ordinary meaning of “processing” described above.

Imbedded in the statutory definition of “processing” is a demonstration of the legislature’s intent when using the term. The definition of “processing” ends by stating that it is “processing by the producer at the production facility.” § 144.054.1(1) (emphasis added); *cf.* § 144.054 (“Additional sales tax exemptions for various industries.”). In isolation, the terms “processing,” “production,” and “facility,” given their broadest possible definitions, could conceivably include almost any activity. But if narrowly construed – as required by law for a tax exemption – and read together, no ordinary Missouri citizen would reach the conclusion that the legislature meant to exempt Casey’s preparation of food. A corner convenience store heating up frozen foods or baking pizzas to go is simply not “processing” at a “production facility.” *See, e.g., Hudson Foods*, 924 S.W.2d at 277 (referring to large industrial “plants” as “processing facilities”).

Furthermore, Chapter 144, which provides for sales and use taxes along with exemptions, actually uses the term “restaurant” in other sections in a way that is both drastically different than the broad meaning suggested by Aquila (and the Commission), and consistent with the plain and ordinary meaning of “processing.” *See* §§ 144.014.2, 144.018.3. Had the legislature intended to include restaurants, or corner convenience stores selling restaurant-type food, within the manufacturing exemptions set forth in § 144.054.2, then it could have easily used the term “restaurant,” just as it did in these other sections. Indeed, the legislature provided a host of exemptions in § 144.030.2, and even added to those in § 144.054 – including “television or radio broadcasting” and “railroad infrastructure.” § 144.054.3. Yet, nowhere in § 144.054, or in § 144.030.2 for that matter, is the term “restaurant” used.

And when the legislature did use the term “restaurant” in § 144.014, it was not used as the tortured and watered-down version suggested by Aquila in an attempt to turn a restaurant or convenience store into a “processing facility.” Instead, the legislature used the common and ordinary meaning for what a restaurant does – “food prepared by such establishment.” § 144.014.2 (emphasis added; *see also* §§ 144.018.3, 144.020.1(6) (noting that in a restaurant meals and drinks are “furnished” or “served” to the public not produced or manufactured). The legislature in fact used the same meaning as Casey’s did when it represented its activities in all of its governmental filings.

In the same chapter, and only a few sections before the one at issue in this case, the legislature uses the term “restaurant” with its commonly accepted meaning – restaurants make “prepared food” and do not manufacture, process, compound, mine, or produce food and drinks in a processing facility. In yet another section of the same chapter, the legislature again addressed restaurants, eating houses, and other places in which “meals, or drinks are regularly served to the public.” § 144.018.3. It is presumed that “the legislature had knowledge of the law, the surrounding circumstances and the purpose and object to be accomplished.” *Pfefer v. Bd. of Police Comm’rs*, 654 S.W.2d 124, 127 (Mo. App. W.D. 1983). Thus, the legislature’s failure to include restaurants or applicable terms for the preparation of restaurant or convenience store food is telling.

The legislature also specifically identified the nature of the business being taxed when imposing sales and use taxes under Chapter 144. Section 144.020.1 imposes sales tax on all sellers for the privilege of engaging in the business of selling tangible personal property or rendering taxable service at retail in Missouri. Section 144.610 imposes the corresponding use tax on persons storing, using, or consuming tangible personal property in this state. Section 144.020.1(6) establishes the rate of tax on the:

[A]mount paid or charged for all rooms, meals and drinks furnished at any hotel, motel, tavern, inn, restaurant, eating house, drugstore, dining car, tourist

cabin, tourist camp or other place in which rooms, meals or drinks are regularly served to the public.]

Id. (emphasis added). There is no exemption, however, using this same language for meals and drinks regularly served to the public.

The very fact that meals and drinks regularly served to the public are singled out for taxation, but not an exemption, indicates that the legislature intended for the nature of the restaurant business to be considered for all sales and use taxation purposes. It would defeat this very purpose to allow a restaurant or convenience store such as Casey's to take advantage of a manufacturing exemption by interpreting the definition beyond recognition when the legislature knew exactly how to tax (or exempt) the preparation of food at a restaurant or convenience store.

Casey's, by regularly serving food and drinks to the general public, is providing a taxable service rather than acting as a manufacturer. The Commission even concedes "that Casey's is primarily a retailer" and "is not a 'manufacturer' as that term is used in § 144.030.2(4) and (5)." (Appdx. A25). And the Commission further acknowledged that these statutes – including § 144.054 – are "for those who manufacture products in this state." (Appdx. A22). The serving of meals and prepared food and drinks to the public, as Casey's does, is not manufacturing or processing; instead, it is providing a taxable service at retail.

Considered in the context of the entire statute, the manufacturing exemption set forth in § 144.054.2 does not contemplate the interpretation or meaning suggested by Aquila or adopted by the Commission. Instead, it is to be strictly construed and intended to cover only those circumstances in which actual manufacturing, processing, compounding, mining, or producing is done, and not the preparation of restaurant food at a corner convenience store and gas station.

The department promulgated two perfectly narrow and strict constructions of § 144.054 in the Code of State Regulations. *See* 12 CSR 10-110.601 (“Electrical, Other Energy and Water as Defined in Section 144.054, RSMo”); 12 CSR 10-110.621 (“Application of Sales Tax Exemption as Defined in Section 144.054, RSMo”). The department’s regulations relating to § 144.054 “‘should not be judicially invalidated except for weighty reasons and are to be sustained unless unreasonable and plainly inconsistent with the [statutes].’” *Utility Service*, 331 S.W.3d at 658-59 (quoting *Purler-Cannon-Schulte, Inc. v. City of St. Charles*, 146 S.W.3d 31, 47 (Mo. App. E.D. 2004)).

The regulations adopted by the department provide that “[a] restaurant preparing food for immediate consumption is not exempt as a manufacturer” 12 CSR 10-110.601(6)(A), and “[a] restaurant preparing food for immediate consumption is not exempt,” 12 CSR 10-110.621(5)(A). These are unquestionably reasonable interpretations given the plain language, context,

and statutory structure of § 144.054. And they provide further support for the common sense interpretation that should apply.

C. The Commission's Broad Interpretation Produces Absurd and Illogical Results Granting Manufacturing Exemptions to Innumerable Businesses.

In addition to the plain language, context, statutory structure, and regulations applicable to § 144.054.2, courts also look at the potential consequences of the proposed interpretation. Thus, for example, if the proposed interpretation produces an absurd or illogical result the court will not adopt that interpretation or meaning. *See Akins*, 303 S.W.3d at 565 (“A court will look beyond the plain meaning of the statute only when the language is ambiguous or would lead to an absurd or illogical result.”) (citing *Spradlin v. City of Fulton*, 982 S.W.2d 255, 258 (Mo. banc 1998)).

As predicted by the Director in her brief in *Brinker*, see Respondent's Brief, 2010 WL 1368397 *19, Aquila seeks to expand manufacturing exemptions beyond any reason or logic. One would have thought that the decision in *Brinker* would have dampened those efforts. It did not. The Commission, instead, decided that *Brinker* did not apply because that case dealt with § 144.030, and § 144.054 is “in addition to” other exemptions. (Appdx. A28).

While it is true that § 144.054.2 is “in addition to” other exemptions, it can certainly be an addition without being mutually exclusive of § 144.030, or reaching the absurd result suggested by Aquila and the Commission. For

example, § 144.054.2 removes the 10% and 25% thresholds in § 144.030.2(12), and adds exemptions for “gas . . . propane, water, coal, and energy sources, chemicals, machinery, equipment, and materials” if used or consumed in manufacturing. Moreover, §144.054 is connected with and similar to the provisions of § 144.030 – even using the same definition of “processing.” The Commission itself found that “the phrase ‘manufacturing, processing, compounding, mining or producing’ is found in § 144.054, the same phrase is found verbatim, in § 144.030.2(12).” (Appdx. A25).

Attempts by Aquila and the Commission to water down the statutory terms fail to account for the most basic rule for tax exemptions – that exemptions are subject to strict construction against the taxpayer. *Armco, Inc.*, 787 S.W.2d at 724. Thus, if there is any doubt as to whether heating up frozen food for retail sale is “processing” at a “production facility,” then the terms should not be interpreted that broadly. Doubt as to the expansive construction of these terms is more than obvious in this case.

Moreover, if the Commission’s interpretation were correct, there are literally thousands of restaurants and convenience stores throughout Missouri that would follow suit seeking exemption from millions and millions of dollars in taxes. It would undermine this Court’s decision in *Brinker*. Everything from Slushies to hotdogs at the local gas station would be fair game for a manufacturing exemption. Indeed, *Brinker*, through a back door, would now obtain a manufacturing exemption, as would movie theaters (e.g. Wehrenberg),

McDonald's, other fast food businesses, and snack bars, for the very machinery, equipment, and materials for which a tax exemption was rejected by this Court in *Brinker*.

A holding that mere preparation of food is enough to constitute "processing" at a "production facility" would have a devastating impact on sales tax revenue, an impact that appears to be intentionally masked by the small refund claim on electricity in this case. After all, § 144.054.2 exempts not only electricity, but also gas, water, "energy sources," chemicals, machinery, equipment, and "materials." Exempting all of these items for any restaurant or convenience store is not the result the legislature intended, and such a broad and unjustified interpretation, even if a conceivable interpretation, should be rejected by this Court.

D. The Commission, and Courts Throughout the Country, Have Uniformly Rejected Similar Efforts to Broadly Construe Manufacturing Exemptions.

In addition to this Court's decision in *Brinker*, the Commission (with the exception of this case), has consistently maintained that a restaurant is not a manufacturer. See *Brinker Mo., Inc. v. Dir. of Revenue*, Case No. 08-0143 RS (Mo. Admin. Hearing Comm'n, October 14, 2009 (Appdx. A38-A62); *Wendy's of Mid-Missouri, Inc. v. Dir. of Revenue*, Case No. RS-79-0222 (Mo. Admin. Hearing Comm'n, July 22, 1982) (Appdx A63-A73). For example, the underlying decision by the Commission in *Brinker* concluded as follows:

[T]he issue in this case is not whether the processes by which Brinker's restaurants prepare food can fit within the definition of manufacturing, but whether that definition is applicable to the entity in which the processes are taking place, that is, a restaurant, the operations of which are geared toward retail sales and service and not toward production.

Brinker, at pg. 14.

In *Wendy's*, the taxpayer prepared meals and drinks in a manner similar to Casey's; the amount of preparation in *Wendy's* was actually much more extensive. Individual hamburger patties were formed from ground beef that arrived in twenty-pound bulk bags. *Wendy's* at pg. 2. The patties were stacked, wrapped in plastic, and returned to refrigerated storage until needed that day. *Id.* Lettuce, tomatoes, and onions were similarly cleaned, sliced and prepared for use on the hamburgers. *Id.* at pg. 3. Chili was made by combining twelve pounds of cooked ground beef, two cans of red beans, a can of tomato mixture, five cans of tomato juice, and a spice packet. *Id.* The chili was cooked from four to six hours and then simmered on the stove so it was always ready to serve. *Id.* Similar steps were followed for preparation of all sandwiches, French fries, soft drinks, and dairy desserts. *Id.* at pgs. 2-3. Despite these extensive activities, the Commission did not consider the activities manufacturing because the activities were still merely preparation of food by a restaurant.

The Commission's decisions in *Brinker* and *Wendy's* recognize that ignoring whether the taxpayer is actually a manufacturer leads to absurd results not intended by the legislature. This is particularly true under § 144.054.2. If the Commission's decision in this case were upheld then every restaurant, convenience store serving coffee, coffee house, bookstore serving coffee, snack bar at any sports event, or other establishment with a coffee pot in its store for serving customers could claim an exemption from the sales tax on its purchases of electricity, gas, propane, water, coal, energy sources, chemicals, machinery, equipment, and materials.

Decisions by the Commission in *Wendy's* and *Brinker*, as well as this Court's decision in *Brinker*, are in accord with numerous other states that have issued decisions finding that restaurants are not manufacturers. For example, in *McDonald's Corp. v. Okla. Tax Comm'n*, 563 P.2d 635, 641 (Okla. 1977), a fast-food restaurant's preparation of food for immediate retail sale was held not to be manufacturing or processing. The Oklahoma court found that McDonald's was primarily in the business of selling at retail its products which consisted of, among other things, hamburgers, fish fillet sandwiches, French fried potatoes, shakes and carbonated soft drinks. *Id.* at 639. The Oklahoma court explained that the preparation or cooking of food is not "generally recognized" as manufacturing or processing. *Id.* at 638.

Massachusetts, likewise, concluded in *York Steak House Sys., Inc. v. Comm'r of Revenue*, 472 N.E.2d 230 (Mass. 1984) that the thawing and cooking

of a steak was not manufacturing. And in *Arizona Dep't of Revenue v. Blue Line Distributing, Inc.*, 43 P.3d 214 (Az. App. Div. 1 2002), the Arizona Court of Appeals held that a restaurant that uses machinery or equipment to make pizza dough from scratch is not commonly understood to be either a manufacturing operation or a processing operation. *Id* at 215. There are many more decisions on this point. *See, e.g., Burger King, Inc. v. State Tax Commission*, 416 N.E.2d 1024 (N.Y. 1980) (harmonizing New York's sales tax law to conclude that the restaurant was not manufacturing); *Roberts v. Bowers*, 162 N.E.2d 858 (Ohio 1959) (holding that a restaurateur was not a manufacturer); *Golden Skillet Corp. v. Commonwealth*, 199 S.E.2d 511 (Va. 1973) ("Common sense tells us that the process of preparing and frying chicken for sale at retail, notwithstanding the novelty of the patented method and cookers used by the franchisees, is not an industrial operation."); *HED, Inc. v. Powers*, 352 S.E.2d 265 (N.C. App. 1987) (holding that a restaurant is not a manufacturer) (citing *Coachman, Inc. v. Norberg*, 397 A.2d 1320 (R.I. 1979); *McDonald's Corp. v. Oklahoma Tax Comm'n*, 563 P.2d 635 (Okla. 1977); *Golden Skillet Corp. v. Commonwealth*, 199 S.E.2d 511 (Va. 1973); and *Roberts v. Bowers*, 162 N.E.2d 858 (Ohio 1959)).

These decisions demonstrate, along with the plain language, context, statutory structure, and applicable regulations, that § 144.054.2 must be limited to a narrow and common sense interpretation. Heating up frozen food and serving meals at a restaurant or corner convenience store such as Casey's is simply not "processing" at a "production facility."

CONCLUSION

For the foregoing reasons, the Administrative Hearing Commission's decision should be reversed.

Respectfully submitted,

CHRIS KOSTER
Attorney General

By: /s/ Jeremiah J. Morgan
Jeremiah J. Morgan
Mo. Bar #50387
Deputy Solicitor General
P.O. Box 899
Jefferson City, MO 65102
(573) 751-1800
(573) 751-0774 (facsimile)
Jeremiah.Morgan@ago.mo.gov

**ATTORNEYS FOR THE DIRECTOR
OF REVENUE**

CERTIFICATE OF SERVICE AND COMPLIANCE

I hereby certify that a true and correct copy of the foregoing was filed electronically via Missouri CaseNet, and served, on October 13, 2011, to:

Bruce Farmer
OLIVER WALKER WILSON, LLC
401 Locust Street
Suite 406
P.O. Box 977
Columbia, MO 65205-0977

Administrative Hearing Commission
Truman State Office Building
P.O. Box 1557
Jefferson City, MO 65102

The undersigned further certifies that the foregoing brief complies with the limitations contained in Rule No. 84.06(b) and that the brief contains 6,756 words.

/s/ Jeremiah J. Morgan
Deputy Solicitor General