

**IN THE
SUPREME COURT OF MISSOURI**

No. SC88943

GREAT SOUTHERN BANK,

Appellant,

v.

DIRECTOR OF REVENUE,

Respondent.

**Petition For Review
From The Administrative Hearing Commission,
The Honorable John J. Kopp, Commissioner**

APPELLANT'S BRIEF

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JURISDICTIONAL STATEMENT

The principal issue before the Court involves the construction of § 144.025.1, RSMo 2000, which provides in relevant part:¹

Notwithstanding any other provisions of law to the contrary, in any retail sale ..., where any article on which sales or use tax has been paid, credited, or otherwise satisfied or which was exempted or excluded from sales or use tax is taken in trade as a credit or part payment on the purchase price of the article being sold, the tax imposed by sections 144.020 and 144.440 shall be computed only on that portion of the purchase price which exceeds the actual allowance made for the article traded in or exchanged, if there is a bill or sale or other record showing the actual allowance made for the article traded in or exchanged.

Specifically, the issue before the Court is whether this provision applies to a transaction involving the exchange of aircraft with a “qualified intermediary,” in a transaction structured to comply with the like kind exchange provisions of § 1031 of the Internal Revenue Code. Thus, the Court’s review of this case will necessarily involve the construction of § 144.025.1, which is a revenue law of the State of Missouri. This Court has exclusive jurisdiction over the issues pursuant to Article V, § 3 of the Missouri Constitution.

¹ All statutory citations are to the Revised Statutes of Missouri of 2000, as amended, unless otherwise noted.

STATEMENT OF FACTS

1. Introduction

This case involves the application of the trade-in provision of the Missouri sales and use tax law, § 144.025, to a transaction involving the exchange of aircraft. The record in this case includes the decision of the Administrative Hearing Commission (L.F. 13-20)(Appendix A3-A13); the transcript of the April 19, 2007 hearing before the Administrative Hearing Commission, a Joint Filing of Stipulated Facts filed by both parties and the exhibits admitted into the record by the Commission, including Joint Exhibits 1 through 4 and Appellant’s Exhibit 5.²

The transaction at issue in this case was structured to comply with the requirements of § 1031 of the Internal Revenue Code (“I.R.C.”).³ Under I.R.C. § 1031, a taxpayer is permitted to defer the recognition of gain from the disposition of an asset for federal income tax purposes provided the asset is exchanged for property of “like kind.” This provision applies only to the *exchange* of property, not the sale and subsequent purchase of replacement property for cash. The exchange transaction may involve a “qualified intermediary,” as in the instant

² Citations to the hearing transcript are “Tr. p.____.” Citations to the Joint Filing of Stipulated Facts are “Stip. ¶ ____.” Citations to exhibits are “Joint Exhibit ____” or “Appellant’s Exhibit ____” as appropriate.

³ The parties requested that the Commission take judicial notice of I.R.C. § 1031 and the relevant federal Treasury Regulations set forth in § 1.1031. See Stip. ¶ 4.

case. The qualified intermediary facilitates the exchange of two items among three other parties by acquiring the two items to be exchanged from their original owners and transferring each item to the party who wishes to acquire it.

In this case, Appellant owned a Beechcraft C90B Aircraft (the “Beechcraft Aircraft” or “relinquished property”), which it transferred in return for a Cessna Citation Jet 9 (C-525) Aircraft, Registration no. N900DS, (the “Cessna Aircraft” or “replacement property”). This exchange was accomplished by assigning Appellant’s contract to sell the Beechcraft Aircraft and Appellant’s contract to purchase the Cessna Aircraft to a qualified intermediary. Appellant then paid the qualified intermediary \$900,000—the difference in price between the two planes. Appellant was not required to pay the full purchase price of the Cessna Aircraft, only the amount in excess of the “trade-in” amount.

2. History of the Case

Appellant paid Missouri use tax to the Director of Revenue (the “Director”) on the net trade-in price of the Cessna Aircraft. The Director conducted an audit of Appellant’s sales and use tax returns and records for the tax periods beginning April 1, 2001 through and including March 31, 2004. Pursuant to this audit, the Director issued a final decision (assessment number 200508005970016) to Appellant on April 1, 2005. This final decision assessed Appellant \$57,400.00 in use tax and \$3,962.97 in interest. The Director did not assess any additions to tax or penalties. The entire assessment was related to Appellant’s purchase of the Cessna Aircraft.

Appellant filed an appeal of this final decision with the Administrative Hearing Commission (the “Commission”) on May 25, 2005. On April 19, 2007, the Commission conducted a hearing during which the parties presented testimony and exhibits. On October 25, 2007, the Commission issued a decision that denied Appellant a trade-in credit on its purchase of the Cessna Aircraft and that upheld the Director’s assessment. Appellant filed this Petition for Review of the Commission’s decision.

3. Aircraft Transaction

Appellant acquired the Cessna Aircraft through a like kind exchange transaction within the meaning of § 1031 of the Internal Revenue Code. Wachovia Bank National Association (“Wachovia”) acted as the qualified intermediary to facilitate the exchange. There is no dispute that Appellant’s disposition of the Beechcraft Aircraft and Appellant’s acquisition of the Cessna Aircraft qualified as a valid like kind exchange for income taxes under I.R.C. § 1031 and Treas. Reg. § 1.1031. Stip. ¶ 16.

The following agreements document and describe Appellant’s transaction:

1. On June 18, 2003, Appellant entered into an agreement to sell the Beechcraft Aircraft to Jet 1, Inc., for \$1,025,000. Jet 1, Inc., is located in Florida. Stip. ¶ 5; Joint Exhibit 1, Exhibit B. Appellant originally purchased the Beechcraft Aircraft in March of 2002, and paid Missouri use tax on the purchase price. Stip. ¶ 6.

2. On June 27, 2003, Appellant entered into a “Purchase Agreement” to purchase the Cessna Aircraft from Scag Engineering, LLC for \$1,925,000. Scag Engineering, LLC is located in Wisconsin. Stip. ¶ 7; Joint Exhibit 1, Exhibit F.

3. On July 9, 2003, Appellant entered into the following agreements:

a. An “Exchange Agreement” with Wachovia Bank, National Association (“Wachovia”). Stip. ¶ 8; Joint Exhibit 1. The Exchange Agreement states:

i. that Wachovia “desires to acquire the ‘Relinquished Property’ [i.e., the Beechcraft Aircraft] in exchange for property of like kind within the meaning of Section 1031 (referred to herein as the ‘Replacement Property’ [i.e. the Cessna Aircraft]).” Joint Exhibit 1.

ii. that “[Appellant] agrees to convey the [Beechcraft Aircraft] to Wachovia and Wachovia agrees to acquire the [Cessna Aircraft] upon the terms and conditions set forth in [the] Agreement.” Joint Exhibit 1.

iii. that “[t]he consideration for the conveyance of the [Beechcraft Aircraft] shall be the exchange by Wachovia of property of ‘like kind’ ... which shall hereafter be acquired by Wachovia as provided in this Agreement (referred to herein as the ‘Replacement Property’). On the date provided for the closing of the sale of the [Beechcraft Aircraft] as set forth in the contract of the sale of the [Beechcraft Aircraft] (the ‘Relinquished Property Closing Date’), [Appellant] shall convey or cause to

be conveyed the [Beechcraft Aircraft] to Wachovia and, in exchange therefore, Wachovia shall, within the time limitations set forth herein, convey the [Cessna Aircraft] to [Appellant], in accordance with the and subject to the terms and conditions of this Agreement.” Joint Exhibit 1.

b. A “Notice of Assignment” Agreement with Jet 1, Inc., related to the Beechcraft Aircraft. Joint Exhibit 1, Exhibit C. The Notice of Assignment informed Jet 1 that all of Appellant’s rights and interest in the contract for sale of the Beechcraft Aircraft had been assigned to Wachovia as qualified intermediary to facilitate a like kind exchange.

c. A “Reassignment and Assumption” agreement with Wachovia Bank relevant to the Beechcraft Aircraft, under which Appellant agreed to assume all of the “obligations, liabilities and indemnities of Wachovia . . . that survive the closing of the transaction contemplated in [the Beechcraft Aircraft purchase agreement].” Stip. ¶ 10; Joint Exhibit 1, Exhibit D.

d. An “Identification of Replacement Property” agreement with Wachovia Bank, National Association. Stip. ¶ 11; Joint Exhibit 1, Exhibit E..

e. An “Assignment” agreement with Wachovia Bank, National Association relevant to the Cessna Aircraft. Stip. ¶ 12; Joint Exhibit 1, Exhibit F.

f. A “Notice of Assignment” agreement with Scag Engineering, LLC relevant to the Cessna Aircraft. Stip. ¶ 13; Joint Exhibit 1, Exhibit G. The Notice of Assignment informed Scag that all of Appellant’s rights and interest in the

contract for purchase of the Cessna Aircraft had been assigned to Wachovia as qualified intermediary to facilitate a like kind exchange.

g. A “Reassignment and Assumption” agreement with Wachovia Bank, National Association relevant to the Cessna Aircraft under which Appellant agreed to assume all of the “obligations, liabilities and indemnities of Wachovia . . . that survive the closing of the transaction contemplated in [the Cessna Aircraft purchase agreement].” Stip ¶ 14; Joint Exhibit 1, Exhibit H.

Appellant’s exchange of the Beechcraft Aircraft for the Cessna Aircraft under these agreements was completed on July 16, 2003. The closing transactions for both the Beechcraft Aircraft and the Cessna Aircraft occurred simultaneously. Joint Exhibit 3. At closing, Appellant paid \$900,000, which included a \$50,000 deposit previously paid to Insured Aircraft Title Service plus an additional \$850,000 in cash, by wire transfer to an escrow account with Insured Aircraft Title Service for the Cessna Aircraft. This \$900,000 was wire transferred to Wachovia.

Appellant made no other cash payments for the Cessna Aircraft.

Appellant’s Exhibit 5. At the same time, Jet 1, Inc. paid \$1,025,000 to Insured Aircraft Title Service, which included a \$25,000 deposit it had previously paid, plus an additional \$1,000,000 in cash. This \$1,025,000 was wire transferred to Wachovia. Wachovia transferred the full \$1,925,000 to Scag Engineering, LLC for the Cessna Aircraft. Appellant’s Exhibit 5. No cash was transferred to Appellant in this transaction.

STATEMENT OF THE ISSUE

Section 144.025 provides that “where any article on which sales or use tax has been paid . . . is taken in trade as credit or part payment on the purchase price of the article being sold, the [sales tax] shall be computed only on that portion of the purchase price which exceeds the actual allowance for the article traded or exchanged, if there is a bill of sale or other record showing the actual allowance made for the article traded in or exchanged.” Appellant contracted to purchase a Cessna Aircraft with a purchase price of \$1,925,000. To obtain it, Appellant exchanged its old aircraft (the Beechcraft Aircraft) and paid \$900,000—the difference in price between the old aircraft and the new one. Appellant previously paid tax on the Beechcraft Aircraft. Appellant purchased the Cessna Aircraft from an out-of-state seller, and the transaction was subject to Missouri use tax. Is Appellant entitled to a reduction under § 144.025 in the tax owed in connection with its purchase of the Cessna Aircraft based on the “trade-in” allowance it received for the old aircraft that was exchanged for the new one?

STANDARD OF REVIEW

The decision of the Administrative Hearing Commission shall be reversed if: (1) it is not authorized by law; (2) it is not supported by competent and substantial evidence; (3) a mandatory procedural safeguard is violated; or (4) it is clearly contrary to the reasonable expectations of the general assembly. Section 621.193; *Concord Publishing House, Inc. v. Director of Revenue*, 916 S.W.2d 186 (Mo. banc 1996). This Court's review of the law is *de novo*. *Zip Mail Services, Inc. v. Director of Revenue*, 16 S.W.3d 588 (Mo. banc 2000). Because §144.025.1 is a tax imposition statute, it must be construed strictly against the taxing authority. Section 136.300.1; *Old Warson Country Club v. Director of Revenue*, 933 S.W.2d 400 (Mo. Banc 1996); *Utilicorp United, Inc. v. Director of Revenue*, 75 S.W.3d 725 (Mo. banc 2001).

POINTS RELIED ON

I. THE ADMINISTRATIVE HEARING COMMISSION ERRED IN RULING THAT APPELLANT WAS NOT ENTITLED TO A TRADE-IN CREDIT PURSUANT TO SECTION 144.025.1 AGAINST THE USE TAX DUE ON APPELLANT’S PURCHASE OF THE CESSNA AIRCRAFT BECAUSE THE DECISION IS NOT AUTHORIZED BY LAW UNDER SECTION 621.193 IN THAT APPELLANT’S BEECHCRAFT AIRCRAFT WAS TAKEN IN TRADE AS CREDIT OR PART PAYMENT OF THE PURCHASE PRICE OF THE CESSNA AIRCRAFT, AND APPELLANT HAD PREVIOUSLY PAID USE TAX ON ITS PURCHASE OF THE BEECHCRAFT AIRCRAFT.

Central Cooling & Supply Co., Inc. v. Director of Revenue, 648 S.W.2d 546 (Mo. 1982)

Fall Creek Construction Co., Inc. v. Director of Revenue, 109 S.W.3d 165 (Mo. banc 2003)

Ronnoco Coffee Company, Inc. v. Director of Revenue, 185 S.W.3d 676 (Mo. banc 2006)

Ryder Student Transportation Services, Inc. v. Director of Revenue, 896 S.W.2d 633 (Mo. banc 1995)

§ 144.025.1

I.R.C. §1031

Treas. Reg. §1.1031(a)-1(a)

Treas. Reg. § 1.1031(k)-1(g)(4)

II. THE ADMINISTRATIVE HEARING COMMISSION ERRED IN RULING THAT THE TRADE-IN CREDIT SET FORTH IN SECTION 144.025.1 DOES NOT APPLY TO THE USE TAX IMPOSED BY SECTION 144.610 BECAUSE THE DECISION IS NOT AUTHORIZED BY LAW UNDER SECTION 621.193 IN THAT SECTION 144.610 INCORPORATES SECTION 144.025 BY REFERENCE, AND THE COMMISSION'S INTERPRETATION OF THE STATUTES IS INCONSISTENT WITH THE LEGISLATURE'S INTENT AND RESULTS IN A VIOLATION OF THE COMMERCE CLAUSE OF THE UNITED STATES CONSTITUTION.

Associated Industries of Mo. v. Lohman, 511 U.S. 641 (1994)

Farm & Home Sav. Ass'n v. Spradling, 538 S.W.2d 313 (Mo. 1976)

Southwestern Bell Telephone Company v. Morris, 345 S.W.2d 62 (Mo. banc 1961)

Southwestern Bell Yellow Pages, Inc. v. Director of Revenue, 94 S.W.3d 388 (Mo. banc 2002)

§ 144.020.1

§ 144.025

§ 144.440

§ 144.610

§ 144.615(1)

Commerce Clause, U.S. Const., art. 1, §8, cl. 3

ARGUMENT

I. THE ADMINISTRATIVE HEARING COMMISSION ERRED IN RULING THAT APPELLANT WAS NOT ENTITLED TO A TRADE-IN CREDIT PURSUANT TO SECTION 144.025.1 AGAINST THE USE TAX DUE ON APPELLANT’S PURCHASE OF THE CESSNA AIRCRAFT BECAUSE THE DECISION IS NOT AUTHORIZED BY LAW UNDER SECTION 621.193 IN THAT APPELLANT’S BEEHCRAFT AIRCRAFT WAS TAKEN IN TRADE AS CREDIT OR PART PAYMENT OF THE PURCHASE PRICE OF THE CESSNA AIRCRAFT, AND APPELLANT HAD PREVIOUSLY PAID USE TAX ON ITS PURCHASE OF THE BEEHCRAFT AIRCRAFT.

This case involves the purchase of a Cessna Aircraft by Appellant. The full purchase price of the Cessna Aircraft was \$1,925,000. To obtain it, Appellant relinquished its old aircraft (the Beechcraft Aircraft) and paid \$900,000—the difference in price between the Cessna and the Beechcraft. Although the transaction involved many other details, these are the key facts. Under the trade-in provision of § 144.025, these facts establish that Appellant is entitled to calculate the use tax on the Cessna Aircraft on “only that portion of the purchase price which exceeds the actual allowance made for the article traded in,” that is, \$900,000.

Section 144.025 requires only that an article be “taken in trade as credit or part payment of the purchase price of the article being sold.” It does not require that the party receiving the item being traded in be the “seller” of the article being purchased. The transaction in which Appellant acquired the Cessna Aircraft was structured as a like kind exchange within the meaning of I.R.C. § 1031. To accomplish the exchange, Appellant entered into an Exchange Agreement with Wachovia Bank, National Association (“Wachovia”), in which Wachovia agreed to act a “qualified intermediary” within the meaning of Treas. Reg. § 1.1031(k)-1(g)(4). Appellant transferred the Beechcraft Aircraft to Wachovia, along with \$900,000. In return, Wachovia transferred the Cessna Aircraft to Appellant. The transfers of the two aircraft were accomplished by assigning to Wachovia Appellant’s rights in the contract to sell the Beechcraft Aircraft to Jet 1 and its contract to buy the Cessna Aircraft from Scag Engineering. As explained in detail below, this resulted in Appellant’s “sale” of the Beechcraft to Wachovia and “purchase” of the Cessna Aircraft from Wachovia.

I.R.C. § 1031 Like Kind Exchanges

Appellant purchased the Cessna Aircraft in a transaction that met the requirements of a “like kind exchange” within the meaning of I.R.C. § 1031.

There are three basic statutory requirements under I.R.C. § 1031:

1. Both the property surrendered and the property received must be held either for productive use in a trade or business, or for investment;

2. The property surrendered and the property received must be of “like kind”; and
3. The exchange must be a reciprocal transfer of properties as distinguished from a sale for cash and repurchase of the replacement property.

See I.R.C. §1031; Treas. Reg. §1.1031(a)-1(a); *Carlton v. United States*, 385 F.2d 238, 241 (5th Cir. 1967); See also *Coastal Terminals, Inc. v. United States*, 320 F.2d 333 (4th Cir. 1963); *Alderson v. C.I.R.*, 317 F.2d 790 (9th Cir. 1963).

The parties in this case stipulated that Appellant’s sale of the Beechcraft Aircraft and purchase of the Cessna Aircraft pursuant to the Exchange Agreement qualified as a like kind exchange under I.R.C. § 1031 and Treas. Reg. § 1.1031. As a reciprocal exchange of properties, this transaction is distinguishable from a transaction involving the sale of an asset for cash and the subsequent reinvestment of the cash in a new asset. By definition, a transaction involving a sale of an asset for cash and the reinvestment of the cash in a new asset is **not** a like kind exchange. Moreover, to meet the requirements of I.R.C. § 1031, the taxpayer that disposes of an asset cannot receive or have the right to receive any of the cash proceeds from the disposition of that asset during the period in which the exchange is being completed. See Rev. Rul. 57-244; Rev. Rul. 90-34; Treas. Reg. §1.1031(k)-1(f) and §1.1031(k)-1(g)(6); *W.D. Haden & Co. v. Commissioner*, 165 F.2d 588 (5th Cir. 1948).

Application of the “Trade-In” Credit Under § 144.025

On the date of Appellant’s purchase of the Cessna Aircraft, § 144.025.1 (as amended by H.B. 600, effective July 1, 2003) provided in relevant part:

1. Notwithstanding any other provisions of law to the contrary, in any retail sale other than retail sales governed by subsections 4 and 5 of this section, where any article on which sales or use tax has been paid, credited, or otherwise satisfied or which was exempted or excluded from sales or use tax is taken in trade as a credit or part payment on the purchase price of the article being sold, the tax imposed by sections 144.020 and 144.440 shall be computed only on that portion of the purchase price which exceeds the actual allowance made for the article traded in or exchanged, if there is a bill of sale or other record showing the actual allowance made for the article traded in or exchanged.

Under the plain language of § 144.025, the trade-in credit applies to any transaction where:

- (1) an article on which sales or use tax has been paid, credited or otherwise satisfied or which was exempted or excluded from sales or use tax is involved;
- (2) the article is taken in trade as a credit; **or**
- (3) the article is taken as part payment on the purchase price of the article being sold.

Section 144.025 directs that where these conditions are met, tax shall be “computed only on that portion of the purchase price which exceeds the actual allowance made for the article traded in or exchanged, if there is a bill of sale or other record showing the actual allowance made for the article traded in or exchanged.”

In the instant case, all the requirements of this statute are present: (1) the Beechcraft Aircraft was an article on which sales or use tax has been paid, credited or otherwise satisfied and (2) it was taken as part payment on the purchase price of the Cessna Aircraft. In addition, the “actual allowance” for the Beechcraft Aircraft that was “exchanged” is well documented in the Exchange Agreement, the exhibits to the Exchange Agreement and the cash paid by the parties at closing.⁴ None of these facts are in dispute. Stip. ¶ 6; Joint Exhibits 1 – 4; Appellant’s Exhibit 5. Finally, it should be noted that in testimony at the hearing conducted on April 19, 2007, Appellant’s Vice President, Larry Larrimore, testified that it was Appellant’s intent and understanding that the Beechcraft

⁴ Specifically, under paragraph 4.2 (a) of the Exchange Agreement, the proceeds from the Beechcraft Aircraft were to be deposited by Wachovia into the “Exchange Account.” As provided by paragraph 4.2 (c), Appellant had no access to these amounts. Paragraph 4.3 (iii) explains that Appellant was required to pay only the difference between the cost of the Cessna Aircraft and the proceeds from the Beechcraft Aircraft.

Aircraft would be disposed of in exchange for the Cessna Aircraft and that this exchange transaction would be viewed as a unified whole. This view was based on Appellant's involvement in prior like kind exchanges, its understanding of the advice given by Wachovia and its understanding of the language of the Exchange Agreement in the instant situation.

These facts demonstrate that tax applies only to that portion of the purchase price of the Cessna that exceeds the allowance for the Beechcraft for which it was exchanged, that is: \$1,925,000 minus \$1,025,000 or \$900,000—the amount of cash Appellant paid to acquire the Cessna. The Director's assessment, which was based on the full purchase price of the Cessna Aircraft is erroneous and should be set aside by this Court.

The Qualified Intermediary was the “Seller” of the Aircraft

Section 144.025 does not require that the party receiving the article that is taken in trade also be the “seller” of the article being purchased. The language of the statute is clear and unambiguous, and should not be construed to include additional requirements. *See Ryder Student Transportation Services, Inc. v. Director of Revenue*, 896 S.W.2d 633 (Mo. banc 1995). If, however, this Court determines this is a relevant factor in this case, it should find that Wachovia “sold” the Cessna Aircraft to Appellant.

Appellant entered into an Exchange Agreement with Wachovia to act as a “qualified intermediary.” A qualified intermediary is a person, who for a fee, acts to facilitate a like kind exchange by: acquiring the relinquished property from a

taxpayer, transferring the relinquished property to a purchaser, acquiring the replacement property, and transferring the replacement property to the taxpayer. Treas. Reg. § 1.1031(k)-1(g)(4).

Under I.R.C. § 1031, the qualified intermediary is considered to have acquired an ownership interest in the relinquished property and is considered to possess an ownership interest in the replacement property prior to the transfers of such properties. The relationship between Appellant and Wachovia was not one of mere principal-agent. *See* Treas. Reg. §1.1031(k)-1(g)(4). Wachovia was deemed to have acquired and transferred the relinquished property and the replacement property involved in a like kind exchange since: (1) it accepted an assignment of the rights to the agreement for the sale of the relinquished property and the acquisition of the replacement property and (2) all parties to the agreement (*i.e.*, the taxpayer, the third party purchaser of the relinquished property and the seller of the replacement property) were notified in writing of the assignment on or before the transfer of property. *See* Treas. Reg. §1.1031(k)-1(g)(4)(i) through §1.1031(k)-1(g)(4)(v). Specifically, Treas. Reg. §1.1031(k)-1(g)(4)(iv) provides:

(B) An intermediary is treated as **acquiring and transferring the relinquished property** if the intermediary ... enters into an agreement with a person other than the taxpayer for the transfer of the relinquished property to that person and, pursuant to that agreement, the relinquished property is transferred to that person, and

(C) An intermediary is treated as **acquiring and transferring replacement property** if the intermediary ... enters into an agreement with the owner of the replacement property for the transfer of that property and, pursuant to that agreement, the replacement property is transferred to the taxpayer.

Treas. Reg. §1.1031(k)-1(g)(4)(v) further explains:

[A]n intermediary is treated as entering into an agreement if the rights of a party to the agreement are assigned to the intermediary and all parties to that agreement are notified in writing of the assignment on or before the date of the relevant transfer of property.

For example, if a taxpayer enters into an agreement for the transfer of relinquished property and thereafter assigns its rights in that agreement to an intermediary and all parties to that agreement are notified in writing of the assignment on or before the date of the transfer of the relinquished property, the intermediary is treated as entering that agreement. If the relinquished property is transferred pursuant to that agreement, the intermediary is treated as having acquired and transferred the relinquished property. (Emphasis added).

The exchange transaction at issue here included assignments of the sales contracts like those described in Treas. Reg. §1.1031(k)-

1(g)(4)(v). The assignment applicable to the Beechcraft Aircraft is found in Article I, Section 1.1(a) of the Exchange Agreement which provides that Appellant “agrees to convey the [Beechcraft Aircraft] to Wachovia and Wachovia agrees to acquire the [Beechcraft Aircraft] upon the terms and conditions set forth in this Agreement.” Joint Exhibit 1. Appellant provided notification to Jet 1, Inc. that it had assigned its rights to the Beechcraft Aircraft contract to Wachovia, and Jet 1, Inc. signed a “Notice of Assignment” in acknowledgement of its consent to the assignment. *See* Joint Exhibit 1, Exhibit C.

The assignment applicable to the Cessna Aircraft is found in Article II, Section 2.3 of the Exchange Agreement which provides that Appellant “shall enter into a contract for the acquisition of the [Cessna Aircraft] (“the [Cessna Aircraft] Contract”) which shall be assigned to Wachovia for use as Replacement Property.” Appellant provided notification to Scag Engineering, LLC, that it has assigned its rights to the Cessna Aircraft contract to Wachovia, and Scag Engineering, LLC, signed the “Notice of Assignment” in acknowledgement of its consent to the assignment. *See* Joint Exhibit 1, Exhibit F.

The Exchange Agreement thus met the requirements of the Treasury Regulations cited above, which means that under the agreement, Wachovia “acquired and transferred” the aircraft between the parties. This transaction constitutes a “sale” under Missouri’s sales and use tax laws. Section 144.010.1(10) defines “sale at retail” as “*any transfer* made by any person

engaged in business as defined herein *of the ownership of*, or title to, tangible personal property to the purchaser, for use or consumption.” (Emphasis added). Likewise, § 144.605(7) defines “sale” as “*any transfer*, barter or exchange *of the title or ownership of* tangible personal property, or the right to use, store or consume the same, for a consideration paid or to be paid.” (Emphasis added). This Court has concluded that a “sale” may occur without “an outright transfer of [full] title or ownership.” *Ronnoco Coffee Company, Inc. v. Director of Revenue*, 185 S.W.3d 676 (Mo. banc 2006) (citing *Weather Guard, Inc. v. Director of Revenue*, 746 S.W.2d 657 (Mo. App. 1988)).

In addition, the agreement between the parties clearly provided that Wachovia “desires to *acquire* the ‘Relinquished Property’ *in exchange for property of like kind* within the meaning of Section 1031 (referred to herein as the ‘Replacement Property.’” Joint Exhibit 1. Article I, section 1.1(a) of the Exchange Agreement states that “[Appellant] agrees to convey the Relinquished Property to Wachovia and Wachovia agrees to acquire the Relinquished Property upon the terms and conditions set forth in [the] agreement.” Joint Exhibit 1. Such “terms and conditions” include those set forth in Article II, section 2.1 of the Exchange Agreement, which provides:

that ‘the consideration for the conveyance of the Relinquished Property shall be the exchange by Wachovia of property of ‘like kind’ ... which shall hereafter be acquired by Wachovia as provided in this Agreement (referred to herein as the ‘Replacement Property’).

On the date provided for the closing of the sale of the Relinquished Property as set forth in the contract of the sale of the Relinquished Property (the ‘Relinquished Property Closing Date’), *[Appellant]* shall convey or cause to be conveyed the Relinquished Property to Wachovia and, in exchange therefore, Wachovia shall, within the time limitations set forth herein, convey the Replacement Property to Owner, in accordance with the and subject to the terms and conditions of this Agreement.” Joint Exhibit 1.

The language in Appellant’s Exchange Agreement is similar to language considered by this Court in *Fall Creek Construction Co., Inc. v. Director of Revenue*, 109 S.W.3d 165 (Mo. banc 2003). In *Fall Creek*, the parties entered into a Purchase Agreement that stated that “Buyer desires to purchase from Seller, and Seller desires to sell to Buyer, the undivided property interest ... in the aircraft.” The parties argued that this Court should ignore the language of the agreement for use tax purposes and instead, consider the “essence of the transaction.” 109 S.W.3d at 170. This Court rejected this argument and found that the transaction constituted a sale under the use tax law. This Court explained:

Clearly this was a complex transaction between sophisticated parties designed to maximize regulatory and tax advantages. However, the mere fact that the purchase agreement was executed along with other agreements does not render the contract ambiguous nor does it change the nature of [the purchaser’s] interest. [A] determination of

the ‘essence of the transaction,’ is necessary only if the contract contains an ambiguity. There is no ambiguity as to [the purchaser’s] purchase of fractional interests in the aircraft; therefore, an ‘essence of the transaction’ analysis is not necessary.

Fall Creek at 170. Likewise in the instant case, it is clear from the terms of the Exchange Agreement that Wachovia sold the Cessna Aircraft to Appellant and accepted the Beechcraft Aircraft as part payment of the purchase price. The terms of this agreement control the use tax consequences of this transaction.

Similarly, in *Central Cooling & Supply Co., Inc. v. Director of Revenue*, 648 S.W.2d 546 (Mo. 1982) the Court ruled that the precise legal form of the transaction between the parties controlled the sales tax consequences of the transaction. The issue before the court was whether the sale of equipment from a subsidiary corporation to its parent was a taxable transaction for purposes of the Missouri sales tax. Central Cooling & Supply Company was formed as a subsidiary of Johnson Furnace Co., Inc., to purchase equipment from certain suppliers that would not deal directly with retail contractors like Johnson. Central Cooling then resold the equipment to Johnson for Johnson’s use in its retail contracting business. Central Cooling had no employees of its own. Central Cooling claimed it did not owe sales tax on the sale of equipment to its parent claiming the transactions with Johnson were merely “interdepartmental transfers.”

The court in *Central Cooling* examined instances where a corporate entity may be disregarded to obtain the “correct result” and stated:

The test [in determining whether to ignore a transaction's form] is whether the arrangement between the two corporations is being employed for a proper purpose. If the purpose served by the arrangement is fair and lawful, then *the legal forms and the relationships are to be observed* and the case determined upon the basis of separate and individual corporate existence. [In this case,] there is no suggestion that the separate incorporation of Central and Johnson was for any other reason than the proper purpose of gaining a business advantage by obtaining supplies at wholesale prices.

Central Cooling at 548 (emphasis added) (citations omitted).

In Appellant's case, there is no dispute that use of the qualified intermediary structure to engage in a like kind exchange transaction is anything but proper. Appellant did receive a federal and state income tax benefit as a result of disposing of the Beechcraft Aircraft and acquiring the Cessna Aircraft through the qualified intermediary, but the existence of this income tax benefit does not support a finding that the qualified intermediary's role in the like kind exchange transaction can be ignored for Missouri use tax purposes. Rather, since the parties to the like kind exchange transaction have intentionally structured the transaction in certain way for legal and federal and state income tax purposes, the parties are bound to respect such structure, and any benefits or detriments that may result, for Missouri use tax purposes. The fact that the structure also results in a trade-in credit benefit for Appellant in this instance does not change this result.

In sum, Wachovia held “ownership of” the Cessna Aircraft and transferred its interest to Appellant in return for the Beechcraft Aircraft and \$900,000.

Wachovia was thus the “seller” of the Cessna Aircraft in the transaction at issue. Because this sale involved the receipt of the Beechcraft Aircraft which was taken in trade and part payment of the purchase price, § 144.025 directs that the use tax be calculated “only on that portion of the purchase price which exceeds the actual allowance made for” the Beechcraft, that is, \$900,000.

Finally, it should be noted that the fundamental tenets of I.R.C. § 1031 support the contention that a like kind exchange should be characterized as a transaction that qualifies for trade-in treatment under § 144.025. The essence of a § 1031 exchange is a *reciprocal transfer of properties*. This is contrasted to a situation involving a sale of property for cash and the reinvestment of such cash to acquire another property. If by its terms, a transaction must be a property for property *exchange* for federal and state income tax purposes, it certainly follows that the transaction at issue is an *exchange* of properties (*i.e.*, a “trade-in”) for purposes of the Missouri use tax law.

II. THE ADMINISTRATIVE HEARING COMMISSION ERRED IN RULING THAT THE TRADE-IN CREDIT SET FORTH IN SECTION 144.025.1 DOES NOT APPLY TO THE USE TAX IMPOSED BY SECTION 144.610 BECAUSE THE DECISION IS NOT AUTHORIZED BY LAW UNDER SECTION 621.193 IN THAT SECTION 144.610 INCORPORATES SECTION 144.025 BY REFERENCE, AND THE COMMISSION’S INTERPRETATION OF THE STATUTES IS INCONSISTENT WITH THE LEGISLATURE’S INTENT AND RESULTS IN A VIOLATION OF THE COMMERCE CLAUSE OF THE UNITED STATES CONSTITUTION.

The Commission found that the trade-in credit in § 144.025 applies to the sales tax imposed by § 144.020.1, and the motor vehicle use tax imposed by § 144.440, but not the “general use tax” imposed by § 144.610. *Great Southern Bank v. Director of Revenue*, Case No.05-0837 RS, (Mo. Admin. Hearing Comm’n, October 25, 2007); Appendix to Appellant’s Brief A3-A13. This conclusion is contrary to the plain language of the sales and use tax statutes, as well as the legislature’s intent in enacting the use tax. In addition, the Commission’s interpretation of these statutes results in discrimination against interstate commerce in violation of the Commerce Clause of the United States Constitution and thus is inconsistent with § 144.615(1) which provides an

exemption from the use tax for property the “state is prohibited from taxing under the constitution or laws of the United States.”

As the Commission correctly noted, because the aircraft was purchased by the Appellant outside Missouri, the transaction at issue in this case is subject to the “general use tax” under § 144.610.1. This section imposes a tax “in an amount equivalent to the percentage imposed on the sales price in the *sales tax law in section 144.020*.” (Emphasis added). Section 144.020, in turn, imposes a tax “equivalent to four percent of the purchase price paid or charged, or in case such sale involves the exchange of property, a tax equivalent to four percent of the consideration paid or charged, including the fair market value of the property exchanged at the time and place of the exchange, *except as otherwise provided in section 144.025*;” (Emphasis added). Thus the tax imposed by § 144.610 incorporates by reference the provisions of § 144.020, which expressly incorporates the trade-in credit of § 144.025. It follows that the trade-in credit of § 144.025 is applicable to the “general use tax” under the plain language of these statutes, and the Commission’s conclusion to the contrary is not supported by law.

The Commission’s conclusion also ignores the fact that “the primary function of a use tax is to complement the sales tax, to supplement and protect the sales tax, to complement the sales tax by *creating equality of taxation* of purchasers on use of property purchased outside the state which cannot be reached as sales because of the commerce clause of the federal constitution.” *Farm & Home Sav. Ass’n v. Spradling*, 538 S.W.2d 313, 317 (Mo. 1976) (emphasis

added), citing *Southwestern Bell v. Morris*, 345 S.W.2d 62, 66 (Mo. banc 1961). This conclusion was reiterated by this Court in *Southwestern Bell Yellow Pages, Inc. v. Director of Revenue*, 94 S.W.3d 388, 392 (Mo. banc 2002), which states that “[t]he use tax complements the sales tax by creating ‘equality of taxation’ among products purchased within and without the state.” In applying this principle, this Court has long held that exemptions from the use tax must precisely mirror the exemptions from the sales tax. See *Southwestern Bell Telephone Company v. Morris*, 345 S.W.2d 62 (Mo. banc 1961). Under the Commission’s ruling, however, this is not the case. Instead, items purchased outside the state in transactions involving a trade-in are subject to a higher tax than identical transactions occurring within the state. There is no “equality of taxation” under this reading of the statutes. For this reason, the Commission’s reading of § 144.025 is inconsistent with the complementary nature of the sales and use taxes and with the principle of “equality of taxation” and must be rejected by this Court.

Finally, the Commission’s conclusion that the trade-in credit in § 144.025 does not apply to the use tax runs afoul of the Commerce Clause of the United States Constitution which prohibits discrimination against interstate commerce. U.S. Const., art. 1, §8, cl. 3; *Associated Industries of Missouri v. Lohman*, 511 U.S. 641 (1994). The United States Supreme Court has concluded that “where the use tax exceeds the sales tax, the discrepancy imposes a discriminatory burden on interstate commerce.” *Associated Industries*, 511 U.S. at 649. This type of

discrimination is prohibited by the Commerce Clause. *Id.* As the Court explained:

The Commerce Clause prohibits economic protectionism—that is, “regulatory measures designed to benefit in-state economic interests by burdening out-of-state competitors.” Thus, we have characterized the fundamental command of the Clause as being that “a State may not tax a transaction or incident more heavily when it crosses state lines than when it occurs entirely within the state[.]”

Id. at 647 (citations omitted). The Commission’s interpretation of §144.025.1 results in the exact type of economic protectionism prohibited by the Commerce Clause since it would allow the trade-in credit in the case of an in-state transaction, while an identical transaction involving an out-of-state seller would be disqualified from receiving the trade-in credit. Such an interpretation impermissibly discriminates against out-of-state sellers in favor of in-state sellers.

Under the use tax statutes, the tax does not apply in instances where it would result in an unconstitutional burden on interstate commerce. Specifically, § 144.615 provides that the “general use tax” does not apply to: “[p]roperty, the storage use or consumption of which this state is prohibited from taxing under the constitution or laws of the United States.” As explained above, the United States Constitution prohibits the state from imposing a higher tax on interstate transactions than on transactions occurring within the state. In-state transactions are subject to the trade-in credit of § 144.025. It follows that under § 144.615 the

use tax does *not* apply to the trade-in value of property exchanged for property that is subject to the use tax. Otherwise, the use tax would apply to “property that this state is prohibited from taxing under the constitution . . . of the United States.”

For these reasons, the Commission erred in ruling that the trade-in credit set forth in § 144.025 applies only to the sales tax, the motor vehicle use tax, but not the “general use tax” of § 144.610. The trade-in credit applies to use tax transactions, including the transaction at issue here.

Conclusion

Appellant purchased the Cessna Aircraft for \$1,925,000. The purchase was accomplished by transferring the Beechcraft Aircraft that was valued at \$1,025,000 and an additional \$900,000 in cash to Wachovia. As a result, under the plain language of § 144.025, Appellant is entitled to a credit against the use tax base applicable to its purchase of the Cessna Aircraft equal to \$1,025,000. No additional state and local use tax or associated interest is due on Appellant's purchase of the aircraft. Accordingly, Appellant requests that this Court find in favor of Appellant, reverse the decision of the Administrative Hearing Commission and abate the use tax and interest assessed against Appellant by the Director.

Respectfully submitted,

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CERTIFICATE OF SERVICE AND COMPLIANCE

The undersigned hereby certifies that on March ____, 2008 two true and correct copies of the foregoing brief, as well as a labeled disk containing the same, were mailed postage prepaid to:

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The undersigned further certifies that the foregoing brief complies with Rule 55.03 and with the limitations contained in Rule 84.06(b) in that it contains 6,965 words, excluding the cover, certificate of service, certificate required by Rule 84.06(c), signature block and appendix.

The undersigned further certifies that the labeled disk filed contemporaneously with the hard copies of this brief has been scanned for viruses and is virus-free.

Scott R. Riley