IN THE MISSOURI SUPREME COURT

NO. SC86347

KIRKWOOD GLASS CO., INC.,

Appellant,

v.

DIRECTOR OF REVENUE, STATE OF MISSOURI,

Respondent.

Appeal from the Administrative Hearing Commission of Missouri

The Honorable June Striegel Doughty, Commissioner

BRIEF OF APPELLANT

McCARTHY, LEONARD, KAMMERER, OWEN, McGOVERN & STRILER, L.C.
James C. Owen, #29604
Katherine S. Walsh, #37255
16141 Swingley Ridge Rd., #300
Chesterfield, MO 63017
(636) 532-7100
(636) 532-0857 (Facsimile)

Attorneys for Appellant

TABLE OF CONTENTS

TABLE OF AUTHORITIES

Cases

Statutes

Rules

Constitutional Provisions

JURISDICTIONAL STATEMENT

This case came before the Administrative Hearing Commission ("AHC") on Appellant's petition seeking review of Respondent's denial of Appellant's application for refund of sales tax paid on purchases of goods inside and outside the City of Kirkwood, Missouri. The parties stipulated to all facts and submitted the case to the AHC on briefs.

This appeal involves the question of whether the current local *use* tax, §§ 144.757 to 144.761, RSMo 2000, when imposed in conjunction with the state *sales* and *use* taxes and the local *sales* tax, violates U.S. Const. Art. I, § 8, cl. 3 (the "Commerce Clause"). Therefore, this appeal involves a construction of the revenue laws of this state and is within the jurisdiction of this Court pursuant to Mo. Const. Art. V, § 3 and §621.189, RSMo 2000.

STATEMENT OF FACTS

On or about January 22, 2003, Appellant Kirkwood Glass Co., Inc. ("Kirkwood Glass") filed its Application for Sales/Use Tax Refund/Credit with Respondent Director of Revenue ("DOR") based on an overpayment of local use taxes. (L.F. 9-23) As reason for the overpayment, Kirkwood Glass stated, in part:

> The local use tax [§§ 144.757 – 144.761, RSMo 2000] violates Article I, Section 8, Clause 3 of the United States Constitution (the "Commerce Clause"), which provides that "Congress shall have Power … To regulate commerce with foreign nations, and among the several states, and with the Indian tribes." The Commerce Clause protects free trade among the states by restricting both state and municipal governments from discriminating against interstate commerce. In short, the local use tax imposes a higher rate of tax on property purchased out-of-state and used in a county or jurisdiction that imposes a local use tax (a "taxing county") than on a similarly used property purchased in state in a county with a lower "total sales tax rate" (state and local sales taxes) than the taxing county's "total use tax rate" (state and local use tax).

(*See, e.g.*, L.F. 10)

On or about June 12, 2003, the DOR denied Kirkwood Glass's application. (L.F. 24) Thereafter, on July 2, 2003, Kirkwood Glass filed a timely appeal of the DOR's denial to the Administrative Hearing Commission. (L.F. 1)

In its Complaint, Kirkwood Glass sought an order of the Commission: (1) reversing the DOR's final decision to deny the refund claim; (2) ordering the DOR to pay the refund plus statutory interest to Kirkwood Glass; and (3) ordering the DOR to pay Kirkwood Glass's reasonable attorneys' fees and expenses pursuant to § 536.087, RSMo 2000 because the denial was not substantially justified and there are no special circumstances to make the award of such fees and expense unjust. (L.F. 4)

The parties agreed to submit the case to the Commissioner on the following stipulated facts (L.F. 32-120):

> 1. Kirkwood Glass Co., Inc. (hereinafter may be referred to as "Kirkwood Glass" [or "Appellant"]), the Petitioner herein, is a Missouri corporation in good standing with its principal Missouri business office located at 300 South Kirkwood Road, Kirkwood, Missouri 63122.
>
> 2. The Director of Revenue of the State of Missouri (hereinafter may be referred to as "Director" [or "Respondent"]), the Respondent herein, is the duly appointed and qualified Director of the Missouri Department of Revenue.
>
> 3. Petitioner is a dual operator that sells window and window accessories at retail and also installs windows as a contractor within the state of Missouri. Plaintiff self-accrues and remits state and local sales or use tax on windows it installs.
>
> 4. Petitioner has purchased tangible personal property for use in its business. Petitioner's purchases from sellers in Missouri were subject to

state and local sales tax. Petitioner's purchases by orders given to and approved by out-of-state sellers and shipped from out-of-state to Petitioner's business location in Missouri were subject to state and local use tax.

6.[sic] Petitioner incurred during the period April 1, 2002, through June 30, 2002, a sales tax in the amount of 7.325 percent on its purchases of tangible personal property in Kirkwood, Missouri. The sales tax consists of state sales tax in the amount of 4.225 percent and local sales tax in the amount of 3.10 percent.

7. Petitioner incurred during the period April 1, 2002, through June 30, 2002, a sales tax in the amount of 4.725 percent on its purchases of tangible personal property in Williamsburg, Missouri. The sales tax consists of state sales tax in the amount of 4.225 percent and local sales tax in the amount of 0.50 percent.

8. Petitioner incurred during the period April 1, 2002, through June 30, 2002, a use tax in the amount of 5.475 percent on its purchase of tangible personal property that is ordered from out-of-state and shipped from out-of-state to its business location in Kirkwood, Missouri. The use tax consists of state use tax in the amount of 4.225 percent and the local use tax in the amount of 1.25 percent.

9. The use tax rate in Williamsburg during the period April 1, 2002, through June 30, 2002, was 4.225 percent, the state use tax rate. There is no local use tax in Williamsburg, Missouri.

10. Attached as Exhibit A (L.F. 36-67) is a complete listing of the sales and use tax rates of all counties and other political subdivisions within the State of Missouri for the period April 1, 2002, through June 30, 2002. Exhibit A is incorporated into and made a part of this Stipulation of Facts.

11. Attached as Exhibit B (L.F. 68-99) is a complete listing of the sales and use tax rates of all counties and other political subdivisions within the State of Missouri for the period January 1, 2004, through March 31, 2004. Exhibit B is incorporated into and made part of this Stipulation of Facts.

12. Kirkwood Glass filed an Application for Tax Refund/Credit with the Respondent on January 22, 2003. A true and correct copy is attached as Exhibit C (L.F. 100-118), which is incorporated into and made part of this Stipulation of Facts.

13. The Director denied Kirkwood Glass's Application for Tax Refund/Credit by Final Decision on June 12, 2003. A true and correct copy is attached as Exhibit D (L.F. 119-120), which is incorporated into and made part of this Stipulation of Facts.

14. Kirkwood Glass filed its Complaint with the Administrative Hearing Commission on July 2, 2003. (L.F. 1-24)

15. The Director filed her Answer with the Administrative Hearing Commission on August 1, 2003. (L.F. 25-31)

16. The Director and Kirkwood Glass disagree that a refund in the amount of $6,371.63 for local use taxes paid on purchases, plus statutory interest, should be granted.

On September 24, 2004, Commissioner June Striegel Doughty filed her decision in this matter. (L.F. 121-135) The Commissioner found that she was without jurisdiction to declare the local use tax statutes unconstitutional and, therefore, denied Kirkwood Glass's application for refund. (L.F. 121) In her conclusions of law, the Commissioner found:

> This Commission does not have jurisdiction to consider constitutional challenges to statutes. *General Motors Corp. v. Director of Revenue*, 981 S.W.2d 561, 563 (Mo. banc 1998). We must apply the statutes as written. *Bridge Data Co. v. Director of Revenue*, 794 S.W.2d 204, 207 (Mo. banc 1990). However, we have a statutory duty to make findings of fact and conclusions of law in cases before us. Section 536.090.
>
> We have made findings of fact based on the stipulations and exhibits. Those findings include a finding that from April 1, 2002, through June 30, 2002, no county or municipality in Missouri imposed a use tax that was higher than its sales tax. In *Associated Indus. of Missouri v. Lohman*, 114 S.Ct. at 1824, the United States Supreme Court noted that some states have devised systems to ensure that use taxes are not higher than sales taxes

within the same taxing jurisdiction. Section 144.757.1 provides that the local use tax shall be at the same rate as the local sales tax. Section 144.757.3 further provides that 'if any local sales tax is repealed or the rate thereof is reduced or raised by voter approval, the local use tax rate shall also be deemed to be repealed, reduced or raised by the same action repealing, reducing or raising the local sales tax.' Therefore, as provided by the terms of the current local use tax statutes, and in actual effect as shown by our findings, the use tax rate was not higher than the sales tax rate within any local taxing jurisdiction from April 1, 2002 through June 30, 2002.

Kirkwood Glass appealed the Director's final decision to this Commission, and it has the burden of proof. Sections 136.300.1 and 621.050.2. The sole claim that Kirkwood Glass has raised in this appeal is that the current local use tax, §§ 144.757 through 144.761, violates the Commerce Clause. U.S. Const. art. 1, §8. Because we cannot declare statutes unconstitutional, *General Motors*, 981 S.W.2d at 563, we do not have jurisdiction to give Kirkwood Glass the relief that it seeks. Therefore, we must conclude that Kirkwood Glass was liable for the local use tax for April 1, 2002 through June 30, 2002, and is not entitled to a refund of local use tax.

(L.F. 134-135)

On October 8, 2003, Kirkwood Glass filed a timely Petition for Review with this Court pursuant to Mo. R. Civ. P. 100.02 and § 621.189, RSM0 2000.

POINT RELIED ON

THE ADMINISTRATIVE HEARING COMMISSION ERRED IN DENYING APPELLANT'S APPLICATION FOR REFUND OF LOCAL USE TAX PAID BECAUSE THE LOCAL USE TAX ENABLING LEGISLATION, §§ 144.757 TO 144.761, RSMo 2000, VIOLATES THE COMMERCE CLAUSE (U.S. CONST. ART. I, § 8, cl. 3), IN THAT DIFFERENT LOCAL TAXING JURISDICTIONS IN MISSOURI HAVE WIDELY VARYING AMOUNTS OF LOCAL USE TAX IMPOSED ON OUT-OF-STATE PURCHASES SO THAT THE OUT-OF-STATE PURCHASERS OF THESE GOODS CAN BE REQUIRED TO PAY MORE TOTAL USE TAX IN THE TAXING JURISDICTION WHERE IT USES SUCH GOODS THAN THE TOTAL SALES TAX IT WOULD PAY IF IT PURCHASED THE SAME GOODS IN MISSOURI IN A NEIGHBORING JURSDICTION WITH A LOWER TOTAL SALES TAX RATE.

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

Halliburton Oil Well Cementing Co. v. Reily, 373 U.S. 64 (1963)

Henneford v. Silas Mason Co., 300 U.S. 577 (1937)

American Modulars Corp. v. Lindley, 376 N.E.2d 575 (Ohio 1978), *cert. denied* 439 U.S. 911 (1978)

U.S. Const. Art. I, § 8, cl. 3

§ 144.747, RSMo Supp. 1990 (repealed prior to enactment)

§ 144.748, RSMo Supp. 1991 (Repealed)

§§ 144.757 to 144.761, RSMo Supp. 1996

Ohio Code § 5741.021

ARGUMENT

SUMMARY OF ARGUMENT

Kirkwood Glass maintains that the current local *use* tax, §§ 144.757 to 144.761, RSMo 2000[1] , when imposed in conjunction with the state *sales* tax, violates U.S. Const. Art. I, § 8, cl. 3 (the "Commerce Clause"). The current local use tax law permits certain local taxing jurisdictions to impose a local use tax equal to the local sales tax rate, in addition to the mandatory 4.225% state use tax. The local use tax must be approved by a majority of the electorate in the county or municipality. § 144.757.1.

Thus, many jurisdictions have not enacted the local use tax and have only a local sales tax in effect. (L.F. 36-99) In addition, § 144.757 states that "[a]ny county or municipality … may, by a majority vote of its governing body, impose a local use tax if a local sales tax is imposed … at a rate equal to the rate of the local sales tax in effect in such county or municipality …." [Emphasis added.] Many jurisdictions have interpreted this language to mean that the local use tax can be equal to or less than the local sales tax. This has created a situation whereby different local taxing jurisdictions throughout the State of Missouri have widely varying amounts of local use tax imposed on out-of-state purchases, or none at all.

The different local use tax rates, if any, have led to a situation whereby Missouri's sales and use tax law, working together impose a greater *total use tax rate* (combined state and local tax) on goods purchased out-of-state and used in a county or jurisdiction

[1] All statutory references are to RSMo 2000 unless otherwise indicated.

that imposes a higher local use tax rate than on similar good purchased in the State in a jurisdiction with a *total sales tax rate* (combined state and local) that is less than the *total use tax rate*. **Kirkwood Glass maintains that this scheme favors in-state purchases over out-of-state purchases where a taxpayer resides in a county or municipality that imposes a local use tax, as the taxpayer can simply buy goods in one of many local jurisdictions that impose a *total sales tax rate* lower than the *total use tax rate*.**

In short, the current local use tax law authorizes *intra*-county tax parity, such that a taxpayer pays the same total use and sales tax within the municipalities and counties enacting the local use tax. However, there is not *inter*-county parity, such that a taxpayer must pay a greater total use tax if it purchases goods from out-of-state in a taxing jurisdiction imposing the local use tax than if that taxpayer went into a neighboring jurisdiction that imposes a lower total sales tax rate than the total use tax rate in the jurisdiction where the goods are used. The end result is that such a taxpayer has an incentive to avoid purchasing goods out-of-state if it can purchase the same goods in-state at a lower total tax rate. This clearly and unequivocally violates the Commerce Clause, which protects free trade among the states by restricting both state and municipal governments from discriminating against interstate commerce.

POINT RELIED ON

THE ADMINISTRATIVE HEARING COMMISSION ERRED IN DENYING APPELLANT'S APPLICATION FOR REFUND OF LOCAL USE TAX PAID BECAUSE THE LOCAL USE TAX ENABLING LEGISLATION, §§ 144.757-144.761, RSMo 2000, VIOLATES THE COMMERCE CLAUSE (U.S. CONST. ART. I, § 8, cl. 3), IN THAT DIFFERENT LOCAL TAXING JURISDICTIONS IN MISSOURI HAVE WIDELY VARYING AMOUNTS OF LOCAL USE TAX IMPOSED ON OUT-OF-STATE PURCHASES SO THAT THE OUT-OF-STATE PURCHASERS OF THESE GOODS CAN BE REQUIRED TO PAY MORE TOTAL USE TAX IN THE TAXING JURISDICTION WHERE IT USES SUCH GOODS THAN THE TOTAL SALES TAX IT WOULD PAY IF IT PURCHASED THE SAME GOODS IN MISSOURI IN A NEIGHBORING JURSDICTION WITH A LOWER TOTAL SALES TAX RATE.

A. STANDARD OF REVIEW

The Administrative Hearing Commission rendered its decision based on its interpretation of the law and the joint stipulation of facts filed by the parties. Review of an interpretation of law is *de novo*. *Oakland Park Inn v. Director of Revenue*, 822 S.W.2d 425 (Mo. banc 1992). The Commission's decision will be upheld if it is authorized by law and supported by competent and substantial evidence on the whole record, unless the result is clearly contrary to the expectations of the general assembly.

Doe Run Resource Co. v. Director of Revenue, 982 S.W.2d 269, 270 (Mo. banc 1999). Nothing in the constitution or the statutes requires that this court view the evidence and all reasonable evidence drawn therefrom in the light most favorable to the Commission's decision denying the refund. *Hampton v. Big Boy Steel Erection*, 121 S.W.3d 220, 223 (Mo. banc 2003); Mo. Const. Art. V, § 18; § 621.193. This is especially true here, where the Commission's denial of Kirkwood Glass's refund application was based on the fact that it was without jurisdiction to rule on the constitutionality of the local use tax statutes. Because the AHC: 1) did not make factual findings but only adopted the parties' stipulated facts; and 2) admitted that it lacked jurisdiction to declare statutes unconstitutional or afford Kirkwood Glass any relief that it requested (L.F. 134-135), any comments by the AHC concerning the application of law to facts in the AHC's conclusions of law should be ignored.

B. HISTORY OF LOCAL USE TAX IN MISSOURI

Prior to 1990, Missouri had a state sales tax rate and an equivalent state use tax rate (4.225%) on all purchases of tangible personal property. The sales tax rate was applied to purchases made within the state and the use tax rate was applied to purchases made outside of the state. The legislature had also enacted enabling legislation, which permitted, but did not require, county and municipal governments to impose a local sales tax on the sale of tangible personal property sold within the taxing jurisdiction in addition to the 4.225% state sales tax. *See, e.g.*, §§ 66.600 to 66.630, 67.500 to 67.545, 92.400 to 92.420, 94.500 to 94.510, 94.600 to 94.655 and 94.700 to 94.745, RSMo 1986. The amount of local sales tax differed from jurisdiction to jurisdiction, so the combined

amount of tax (state sales tax plus local sales tax) on purchases made within the state could differ from jurisdiction to jurisdiction. As a result, local sales tax rates varied from .5% to 2.0%. The statewide average was approximately 5.725% combined state and local sales tax. During this time period, the only use tax in force was the state use tax rate of 4.225%.[2]

In August 1990, the Missouri legislature passed § 144.747, RSMo Supp. 1990, the original local use tax law (hereinafter "the 1990 Law"). This provision stated: "Other provisions of law notwithstanding, whenever a political subdivision is authorized to levy a sales tax, the political subdivision shall also be authorized to levy a use tax at the same rate which shall be applied in the same manner as the state use tax pursuant to chapter 144." However, this law was repealed prior to enforcement.

In August 1991, the Missouri legislature passed another local use tax law (hereinafter "the 1991 Law"), § 144.748 (now repealed), which stated, in pertinent part:

> 1. In addition to the taxes imposed by section 144.610 [the "state use tax"], there is hereby imposed an additional use tax in the amount of one and one-half percent on all transactions which are subject to the taxes imposed under sections 144.600 to 144.745. This tax shall be

[2] These facts are set out in *Associated Industries of Missouri v. Director of Revenue*, 857 S.W.2d 182, 184-85 (Mo. banc 1993), *rev'd sub nom Associated Industries of Missouri v. Lohman*, 511 U.S. 641 (1994).

collected and remitted together with the taxes imposed under sections 144.600 to 144.745.

Unlike the 1990 Law, which permitted counties and municipalities to adopt their own local use tax at the same rate as the local sales tax, the 1991 Law imposed an additional, flat, statewide local use tax rate of 1.5% on the sales price of tangible personal property purchased outside the state to be stored, used or consumed within the State of Missouri.

The legislature's 1991 enactment of § 144.748 created a uniform *total use tax rate* (state and local) of 5.725% on all transactions. The *total sales tax rate* could be higher or lower than the uniform combined state and local use tax rate of 5.725%, which created a situation where, depending on the particular jurisdiction, out-of-state purchases were taxed higher than in-state purchases.

In 1992, the 1.5% flat local use tax was challenged by Associated Industries of Missouri ("AIM") and certain taxpayers who paid sales and use taxes on the basis that § 144.748 was, *inter alia*, unlawful and violated the Commerce Clause and the Hancock Amendment (Mo. Const. Art. X, §§ 16-23). The suit was brought in Cole County, Missouri. The circuit court found that § 144.748 did not discriminate against interstate commerce. *Associated Industries of Missouri v. Wagner*, No. CV192-15CC (Cir. Ct. of Cole County, MO 7/15/92).

An appeal was taken to this Court, which affirmed the circuit court decision. This Court reasoned that the mandatory 1.5% local use tax might be discriminatory in jurisdictions where the local use tax exceeded the local sales tax, but that the statewide effect of the law was, overall, one that did not favor in-state purchases, as there were still

more sales taxes than use taxes raised statewide (because so many large taxing jurisdictions had local sales tax rates above 1.5%. *Associated Industries of Missouri v. Director of Revenue*, 857 S.W.2d 182, 192 (Mo. banc 1993) (*"AIM I"*).

In a strongly worded dissent, Judge Robertson disagreed with the majority decision, stating:

> A fair reading of the relevant cases, I believe, compels the conclusion that there is no de minimis exception to the Commerce Clause. The duty exacted by a state must be the same whether the goods subject to taxation originated in state or out-of-state - - all of the time and in all of the state. Such a result is consistent with the view announced in *Quill Corp.* [*v. North Dakota*, 504 U.S. 298 (1992)] that a 'bright-line rule in the area of sales and use taxes also encourages settled expectations and, in doing so, fosters investment by businesses and individuals.'

Id. at 199 (Robertson, J. dissenting). [Emphasis added; some citations omitted.]

AIM appealed to the United States Supreme Court, which ultimately agreed with Judge Robertson[3] and found that, in those localities where use tax exceeded sales tax, the local use tax scheme established in § 144.748 impermissibly discriminated against interstate commerce. *Associated Industries of Missouri v. Lohman*, 511 U.S. 641, 654

[3] The author, Justice Clarence Thomas, even quoted Judge Robertson's remark that the Missouri Supreme Court majority had determined that the constitution was similar to the cliché - - "close enough for government work." 511 U.S. at 646.

(1994) ("*AIM II*"). The United States Supreme Court neither upheld nor invalidated § 144.748 *ab initio* but, rather, remanded the case back to this Court for determination of the appropriate remedy. *Id*. at 653.

On July 5, 1994, this Court remanded the case back to the Circuit Court of Cole County, which found that its jurisdiction was limited by the United States Supreme Court's mandate. The Cole County Court erroneously believed that this mandate only allowed for the determination of an appropriate remedy.

A new appeal was taken to this Court, which finally declared that §144.748 was unconstitutional and void *ab initio*. *Associated Industries of Missouri v. Director of Revenue*, 918 S.W.2d 780, 785 (Mo. banc 1996), *as mod. on denial of r'hrg* ("*AIM III*"). In that opinion, Judge Limbaugh made the following finding:

> Prior to the enactment of § 144.748, the General Assembly had enacted § 144.747,[4] which gave counties and municipalities the option of levying a local use tax equal to their local sales tax. Had § 144.747 actually been implemented, the potential result would have been a wide variety of local use taxes across the state, some jurisdictions having them, and some not. The statute was never implemented, however, and was ultimately repealed and replaced with § 144.748, a uniform statewide tax, which had the significant advantage that it would be much less difficult to administer.

[4] Section 144.747, is quoted on p. 18, supra.

> In view of the Supreme Court's ruling, § 144.748 is reduced to something similar to what had previously been rejected, **a patchwork tax scheme** in which some jurisdictions have a use tax, and some do not.

Id. at 785. [Underlined and bold emphasis added.]

Thereafter, the Missouri legislature repealed §144.748 and enacted the current system, §§ 144.757 to 144.761, RSMo Supp 1996 (hereinafter "the 1996 Law" or "the Current Law"). It provides, in part:

> Any county or municipality, except municipalities within a county of the first classification with a population in excess of nine hundred thousand may, by a majority vote of its governing body, impose a local use tax if a local sales tax is imposed as defined in section 32.085, RSMo, at a rate equal to the rate of the local sales tax in effect in such county or municipality, provided, however that no ordinance or order enacted pursuant to sections 144.757 to 144.761 shall be effective unless the governing body of the county or municipality submits to the voters thereof at a municipal, county or state general, primary or special election prior to August 7, 1996, or after December 31, 1996, a proposal to authorize the governing body of the county or municipality to impose a local use tax pursuant to sections 144.757 to 144.761. Municipalities within a county of the first classification having a charter form of government with a population in excess of nine hundred thousand may, upon voter approval received pursuant to paragraph (b) of subdivision (2) of subsection 2 of this

> section, impose a local use tax at the same rate as the local municipal sales tax with the revenues from all such municipal use taxes to be distributed pursuant to subsection 4 of section 94.890, RSMo. The municipality shall within thirty days of the approval of the use tax imposed pursuant to paragraph (b) of subdivision (2) of subsection 2 of this section select one of the distribution options permitted in subsection 4 of section 94.890, RSMo, for distribution of all municipal use taxes.

§ 144.757.1, RSMo. Under this current legislation, the same as the originally enacted but never implemented 1990 Law, § 144.747, some municipalities have enacted a local use tax and some have not. Where enacted, the amount of local use tax is equal to the amount of local sales tax in the jurisdiction but the amount of local use tax varies from jurisdiction to jurisdiction. (This was also the case with the original § 144.747, a statute deemed "a patchwork scheme" by Judge Limbaugh in *AIM III*, 918 S.W.2d at 785.)

C. THE CURRENT LOCAL USE TAX IS ALSO UNCONSTITUTIONAL

Kirkwood Glass maintains that the 1996 Law also violates the Commerce Clause.[5] "It has long been established that the Commerce Clause of its own force protects free trade among the States. One aspect of this protection is that a State 'may not discriminate between transactions on the basis of some interstate element.' That is, a State may not

[5] As noted earlier, U.S. Const. Art. I, § 8, cl. 3 provides that: "Congress shall have Power … To regulate commerce with foreign nations, and among the several states, and with the Indian tribes."

tax a transaction or incident more heavily when it crosses state lines than when it occurs entirely within the State." *Armco, Inc. v. Hardesty*, 467 U.S. 638, 642 (1984). [Citations omitted.] Equal treatment for all taxpayers, similarly situated, is the condition precedent for a valid use tax. *Halliburton Oil Well Cementing Co. v. Reily*, 373 U.S. 64, 69 (1963).

The current legislation permits county and municipal jurisdictions to impose a local use tax equal to the amount of its local states tax. It is a statute almost identical to § 144.747, the predecessor to § 144.748, which was repealed before it was ever enforced and which this Court opined constituted a "patchwork scheme in which some jurisdictions have a use tax, and some do not." Moreover, even though the current local use tax was intended to be equal to the local sales tax, the evidence shows that many local jurisdictions, perhaps because of the need for the tax to pass by a majority vote, have passed local use taxes in an amount less than the local sales tax or not at all. (L.F. 36-99) Although the Missouri legislature's passage of §§ 144.757-144.761 was an attempt to remedy the infirmities found in the previous enactment (§144.748), that attempt has failed, because the local use tax now in effect continues to violate the Commerce Clause even more egregiously.

1. <u>Standard for Analysis of State Economic Regulation</u>

The United States Supreme Court has adopted a two-tier approach to analyzing state economic regulation under the Commerce Clause.

> When a state statute directly regulates or discriminates against interstate commerce, or when its effect is to favor in-state economic interests over out-of-state interests, we have generally struck down the statute without

> further inquiry. See, *e.g.*, *Philadelphia v. New Jersey*, 437 U.S. 617, 98 S.Ct. 2531, 57 L.Ed.2d 475 (1978); *Shafer v. Farmers Grain Co.*, 268 U.S. 189, 45 S.Ct. 481, 69 L.Ed. 909 (1925); *Edgar v. MITE Corp.*, 457 U.S. 624, 640-643, 102 S.Ct. 2629, 2639-2641, 73 L.Ed.2d 269 (1982)(plurality opinion.) When, however, a statute has only indirect effects on interstate commerce and regulates evenhandedly, we have examined whether the State's interest is legitimate and whether the burden on interstate commerce clearly exceeds the local benefits. *Pike v. Bruce Church, Inc.*, 397 U.S. 137, 142, 90 S.Ct. 844, 847, 25 L.Ed.2d 174 (1970). We have also recognized that there is no clear line separating the category of state regulation that is virtually *per se* invalid under the Commerce Clause, and the category subject to the *Pike v. Bruce Church* balancing approach. In either situation the critical consideration is the overall effect of the statute on both local and interstate activity. See *Raymond Motor Transportation, Inc. v. Rice*, 434 U.S. 429, 440-441, 98 S.Ct. 787, 793-94, 54 L.Ed.2d 1664 (1978).

Brown-Forman Distillers Corp. v. New York State Liquor Authority, 476 U.S. 573, 579 (1986). Here, the local use tax directly discriminates against interstate commerce and favors in-state over out-of-state interests. As explained in the next section, the overall effect of the current local use tax is "direct discrimination" against interstate commerce and it should, therefore, be struck down in its entirety, allowing Kirkwood Glass to obtain its refund.

2. The Issue of Equality

"[E]quality for the purposes of competition and the flow of commerce is measured in dollars and cents, not legal abstractions." *Halliburton*, 373 U.S. at 70. A state tax is assessed in light of its actual effect considered in conjunction with other aspects of the State's taxing scheme. *Maryland v. Louisiana*, 451 U.S. 725, 756 (1981). Here, when viewed as a whole, the local use tax does not provide for equality between those who buy products within the state as opposed to those who purchase goods out-of-state. The facts, as stipulated by the parties, conclusively demonstrate this inequality.

Kirkwood Glass incurred sales tax of 4.725% on its purchases of tangible personal property in Williamsburg, Missouri. (L.F. 33) In Williamsburg, the state sales tax is equal to 4.225% and the local sales tax is equal to 0.50%. (Id.) At the same time, Kirkwood Glass paid a use tax of 5.475% on its purchases of tangible personal property, ordered from out-of-state and shipped to its business location in Kirkwood Missouri. (Id.) In Kirkwood, the state use tax is equal to 4.225% and the local use tax is equal to 1.25%. (Id.) Kirkwood Glass, therefore, pays more use tax (for out-of-state purchases) in Kirkwood, Missouri than its pays sales tax (for in-state purchases) in Williamsburg, Missouri. The inequality exists between the taxing jurisdictions. While it may be true that within each individual taxing jurisdiction local use tax does not exceed local sales tax, the local use tax still does not provide for the equality guaranteed by the Commerce Clause. Any other interpretation would mean that the Commerce Clause of the United States Constitution has fallen into control of local municipalities.

As an example, if Kirkwood Glass wanted to purchase $100,000 worth of a good to be used in Kirkwood from out-of-state because it preferred that vendor, it would have to pay $5,475.00 in total use tax ($100,000 X 5.475%). The same purchase from Williamsburg, Missouri would result in total sales tax of $4,725.00 ($100,000 X 4.725%). It would behoove Kirkwood Glass to purchase that good in Williamsburg and save the $750.00.

A review of Exhibits A, B and C to the Joint Stipulation of Facts (L.F. 36 – 118) demonstrates that the local use tax in the City of St. Louis is greater than the local sales tax in seventy five (75) of the taxing jurisdictions within St. Louis County. Thus, it is easy to see how a taxpayer purchasing goods out-of-state and using them within the City of St. Louis is taxed at a greater rate than if that same taxpayer merely crossed the city boundary and purchased those same goods in any of those nearby 75 taxing jurisdictions.

The United States Supreme Court has declared that "we have characterized the fundamental command of the [Commerce] 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,' *Armco v. Hardesty*, 467 U.S. 638, 642, 104 S.Ct. 2620, 2622, 81 L.Ed.2d 540 (1984), and have applied a 'virtually *per se* rule of invalidity' to provisions that patently discriminate against interstate trade, *Philadelphia v. New Jersey*, 437 U.S. 617, 624 (1978)." *AIM III*, 511 U.S. at 647. *See also Henneford v. Silas Mason Co.*, 300 U.S. 577, 584 (1937).

The Court in, *Henneford*, 300 U.S. at 584, said it best, when it summarized the theory of a compensatory tax to be one that "[w]hen the account is made up, the stranger

from afar is subject to no greater burdens … than the dweller within the gates. The one pays upon one activity or incident and the other upon another, but the sum is the same when the reckoning is closed. … [E]qual treatment for in-state and out-of-state taxpayers similarly situated is the condition precedent for a valid use tax on goods imported from out-of-state." *Halliburton*, 373 U.S. at 69. This virtual *per se* rule should be applied in the present case, as there is no doubt that the **out-of-state sales transactions involved here within Kirkwood were taxed more heavily than the in-state sales in Williamsburg**.

The Ohio Supreme Court has ruled on a case almost identical to the case at bar. In *American Modulars Corp. v. Lindley*, 376 N.E.2d 575 (Ohio 1978), *cert. denied* 439 U.S. 911 (1978), the Court struck down a law that authorized Ohio counties to impose the same local sales and use tax rates such that there was *intra*-county tax parity.[6] However, this created a situation where there was not *inter*-county parity, such that a taxpayer would pay 4.5% use tax if it purchased the goods in a jurisdiction imposing the local use

[6] Ohio Code §5741.021 provided, in pertinent part: "* * * (A)ny county which levies a tax pursuant to section 5739.021 of the Revised 577 Code (the county sales tax provision) shall levy a tax at the same rate levied pursuant to section 5739.021 of the Revised Code * * * and, in addition to that imposed by section 5741.02 of the Revised Code, on the storage, use, or other consumption in the county of tangible personal property which is subject to the tax levied by this state as provided in section 5741.02 of the Revised Code."

tax, yet the same taxpayer could go to a neighboring county that did not impose a local sales tax and pay .5% less in total sales tax. *Id*. at 576.

The Ohio Supreme Court found that a law that caused a taxpayer to pay a higher total use tax rate on goods purchased out-of-state than on similarly used property purchased in the state, but purchased in a different county, violated the Commerce Clause. *Id*. at 577. Unlike the Missouri legislature, the Ohio legislature changed the local sale and use tax law so as to provide for "equalization" of local taxes depending on the destination of final use of the goods by the taxpayers. Conversely, Missouri's legislature only compounded the problem after § 144.748 was repealed when it enacted a new law that mirrored the one struck down in *American Modulars*.

Interestingly, the majority opinion in *AIM I,* which upheld the previously existing local use tax law (overruled in *AIM II*) distinguished *American Modulars,* stating:

> The state might also have required that the use tax mirror the permissive local sales tax. Neither opinion, however, would guarantee a better result. *American Modulars* illustrates that even these types of statutes are subject to criticism, as residents of one county may travel to another for tax advantage purchases. Depending on the actual tax rates, demographics, and purchasing patterns, they might even result in **greater discrepancies**.

857 S.W.2d at 192. [Underlined and bold emphasis added.] This Court was correct in its assessment of the 1990 Law, which mirrors the Ohio law that was ruled unconstitutional, as this 1990 Law definitely permits "greater discrepancies" than the 1991 use tax law that was struck down in its entirety. Thus, because the 1996 Law is effectively the same as

both the 1990 Law and the Ohio law, this Court's comments regarding "greater discrepancies" must apply to the 1996 Law as well.

Again, in *AIM III*, Judge Limbaugh referred to the original 1990 local use tax statute in Missouri, which was never implemented and which is nearly identical to both the present local use tax law and the Ohio law in *American Modulars* (except that it did not require voter approval), as a "patchwork scheme." *AIM III*, 918 S.W.2d at 785. After the 1991 Law was struck down, it is obvious that the counties and municipalities were crying to the General Assembly to replace this lost revenue. However, even though this Court recognized that the original local use tax would have resulted in "greater discrepancies" than the 1991 Law that was struck down and would have permitted a "patchwork scheme" with "a wide variety of local use taxes across the state," the legislature chose to replace the 1991 Law with nothing more than a retread of the 1990 Law. Kirkwood Glass asserts that this Court recognized, in *AIM I and AIM III*, that a local use tax such as the current version should be avoided because it is inherently problematic. Clearly, the legislature did not conduct an investigation into the proper way to enact a local compensating use tax such as the one enacted in Ohio after the *American Modulars* case.

As noted earlier, the United States Supreme Court succinctly stated the importance of equality in the context of interstate commerce:

> When the account is made up, the stranger from afar is subject to no greater burdens as a consequence of ownership than the dweller within the gates. The one pays upon one activity or incident, and the other upon another, <u>but</u>

> the sum is the same when the reckoning is closed. Equality exists when the chattel subjected to the use tax is bought in another state and then carried into Washington. It exists when the imported chattel is shipped from the state of origin under an order received directly from the state of destination. In each situation the burden borne by the owner is balanced by an equal burden where the sale is strictly local.

Henneford, 300 U.S. at 584. Missouri has completely ignored the equality aspect of the Commerce Clause by enacting a system that, on its face, discriminates against interstate commerce.

The fact that discrimination is not found within each county or municipal taxing jurisdiction does not mean that the local use tax complies with the Commerce Clause. The tax is discriminatory if it "'tax[es] a transaction or incident more heavily when it crosses state lines than when it occurs entirely within the State.'" *Fulton Corp. v. Faulkner*, 516 U.S. 325, 331 (1996), *citing Chemical Waste Management, Inc. v. Hunt*, 504 U.S. 334, 342 (1992). The key is whether there has been discrimination of interstate transactions, it does not matter whether the transaction is equal within a specific county or municipal taxing jurisdiction. "[A]ctual discrimination, wherever it is found, is impermissible, and the magnitude and scope of the discrimination have no bearing on the determinative question whether discrimination has occurred." *Id*. at 333, *citing Maryland v. Louisiana*, 451 U.S. at 760. A State (or any of its political subdivisions) may not avoid the Commerce Clause by "curtailing the movement of articles of commerce through the

subdivisions of the State rather than through the State itself." *Fort Gratiot Sanitary Landfill, Inc. v. Michigan Dept. of Natural Resources*, 504 U.S. 353, 361 (1992).

3. Discrimination Need Not Be Widespread

The discrimination here is patent and obvious. It is, therefore, not necessary for Kirkwood Glass to show that the discriminatory effect is great or widespread.[7]

> Our cases, however, indicate that where discrimination is patent, as it is here, neither a widespread advantage to in-state interests nor a widespread disadvantage to out-of-state competitors need be shown. For example, in *Bacchus Imports, Ltd. v. Dias*, [468 U.S. 263], we held unconstitutional under the Commerce Clause a special exemption from Hawaii's liquor tax for certain locally produced alcoholic beverages (okolehao and fruit wine), even though other locally produced alcoholic beverages were subject to the tax …. And in *Lewis v. BT Investment Managers, Inc.*, [447 U.S. 27], we held unconstitutional a Florida statute that excluded from certain business activities in Florida not all out-of-state entities, but only out-of-state bank holding companies, banks or trust companies. In neither of these cases did we consider the size or number of the in-state businesses favored or the out-of-state businesses disfavored relevant to our determination. Varying the strength of the bar against economic protectionism according to the size

[7] "[T]here is no *de minimis* exception to the Commerce Clause." *AIM I*, 857 S.W.2d at 199.

> and number of in-state and out-of-state firms affected would serve no purpose except the creation of new uncertainties in an already complex field.

New Energy Co. of Indiana v. Limbach, 486 U.S. 269. 276 (1988).

The fact that the discrimination under § 144.757 may not be widespread should not alter the analysis. There is discrimination, patent on the face of the local use tax law, which should be remedied. Kirkwood Glass has demonstrated that the tax discriminates against interstate commerce and should, therefore, be voided.

4. <u>Damages</u>

In footnote 3 of the AHC's decision it notes that, although Kirkwood Glass requested a refund of $6,371.63 for the period September 1999 through June 2002, the parties' Stipulation did not provide any facts for periods before April 2002. In fact, paragraphs 6–8 of the Stipulation dealt only with the three month period between April and June 2002 because that is the only period for which there was direct evidence of a purchase in two different counties that clearly and unequivocally violated the Commerce Clause. In other words, if Kirkwood Glass had purchased the goods in question, as stipulated, in Kirkwood as opposed to Williamsburg, it would have paid more in local use tax on that purchase. What the AHC failed to consider was, if the 1996 Law is set aside *ab initio*, Kirkwood Glass will be entitled to the entire amount of tax in its refund application, because the law supporting the imposition of that tax would be void. The refund application with the amount in that application, $6,371.63, is set out in paragraph

12 of the Stipulation, and that amount should be refunded if the current tax is deemed void.

CONCLUSION

Unlike the first local use tax challenge, where there were hundreds of tax appeals in which refunds were being sought awaiting the *AIM III* decision (and more filed thereafter), there are very few tax appeals pending at the AHC pending a decision in this case.[8] St. Louis County never even passed the current local use tax, nor did many other taxing jurisdictions. Among those appeals on file, the refunds requested are minimal.

The primary reason for the filing of this action was to make the legislature "get it right." There are ways to accomplish that goal consistent with Interstate Commerce and which can generate more revenue than the current law if enacted properly. For all of the reasons stated above, the current local use tax law is unconstitutional.

McCARTHY, LEONARD, KAEMMERER,
OWEN, McGOVERN & STRILER, L.C.

By:_____

James C. Owen, #29604
Katherine S. Walsh, #37255
16141 Swingley Ridge Rd., #300
Chesterfield, MO 63017
(636) 532-7100;
(636) 532-0857 (Fax)
Attorneys for Appellant

[8] The undersigned counsel filed the first mandamus action seeking refunds of the statewide, 1991 local use tax law after *AIM III* in *St. Charles County v. Director of Revenue*, 961 S.W.2d 44 (Mo. banc 1998).

CERTIFICATE OF COMPLIANCE

The undersigned counsel of record hereby certifies that:

1. As required by Rule 55.06, counsel for Appellant are James C. Owen and Katherine S. Walsh, McCarthy, Leonard, Kaemmerer, Owen, McGovern & Striler, L.C., 16141 Swingley Ridge Road, Suite 300, Chesterfield, Missouri 63017, (636) 532-7100, (636) 532-0857 (fax).

2. The Brief to which this certificate is attached complies with the limitations contained in Rule 84.06(b).

3. This Brief contains 7, 969 words in Microsoft Word 2003 format.

4. Also served and filed with this Appellant's Brief is a floppy disk containing the brief, which is double-sided, high density, IBM-PC compatible 1.44 MB, 3½" size, with an adhesive label affixed identifying the caption of the case, the filing party, the disk number, and the word processing format (Microsoft Word 2003). The disk has been scanned for viruses and it is virus-free.

CERTIFICATE OF SERVICE

The undersigned hereby certifies that two true and accurate copies of the foregoing Appellant's Brief, and one disk containing the same, were mailed, postage prepaid, this 30th day of December, 2004 to the following:

Mr. James R. Layton
State Solicitor
Supreme Court Building
207 West High Street
Jefferson City, MO 65102
(573) 751-1800
(573) 751-0774 (Fax)

Mr. Roger Freudenberg
Missouri Dept. of Revenue
Truman State Office Bldg.
301 W. High, Rm. 670
P.O. Box 475
Jefferson City, MO 65105-0475
573-751-4450
573-751-7151 (Fax)