IN THE SUPREME COURT OF MISSOURI
No. SC 97582

INTERVENTIONAL CENTER FOR PAIN MANAGEMENT,

Appellant,

v.

DIRECTOR OF REVENUE,

Respondent.

Appeal from the Administrative Hearing Commission of Missouri
The Honorable Renee T. Slusher, Commissioner

REPLY BRIEF OF APPELLANT INTERVENTIONAL CENTER FOR PAIN MANAGEMENT

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This is not, as the Director's brief argues, a case about who qualifies as a manufacturer under the use tax exemption, or whether the Center is an industrial manufacturer. In addition to the fact that nothing in section 144.054 limits the exemption solely to manufacturers, "manufacturing" is only one of five disjunctive activities that may be exempt under section 144.054.2: "materials used or consumed in the manufacturing, processing, compounding, mining, ***or*** producing of any product."

The Center's status as a manufacturer under section 144.054.2 is irrelevant so long as the items it seeks to exempt from use tax are materials used or consumed in compounding products. As to that question, the Administrative Hearing Commission found that the Center indeed compounds products, but that the items used to do so were not "materials" under section 144.054.2. This was incorrect and the decision of the Commission should be reversed and the case remanded.

I. The term "materials" is not limited to raw materials.

While the Director argues that this Court in *E & B Granite* defined "materials" as raw product from which something is made, the Court did not expressly limit the definition of materials to only raw materials. *E & B Granite, Inc. v. Dir. of Revenue*, 331 S.W.3d 314, 318 (Mo. banc 2011). This Court noted that "'materials' means either (1) the raw product from which something is made or (2) an apparatus necessary to make something." *Id*. (emphasis added).

In what appears to be the inverse of the Director's argument in this case, the Director in *E & B Granite* urged this Court to limit the term "materials" to only an

apparatus necessary to make something, not raw materials. *Id*. The Court rejected that argument, holding that prior courts interpreting section 144.054 did not use the term "material" to refer to an apparatus. *Id*.

The Director in this case incorrectly claims that the Court in *E & B Granite* "rejected" the apparatus definition of materials. But the only thing this Court rejected was the Director's request to limit the definition of "materials" in section 144.054.2 to only apparatuses. The Court did not foreclose the possibility that the definition of materials in section 144.054.2 may also include apparatuses or things other than raw materials. Instead, it can be inferred that *E & B Granite* contemplates that "materials" may be both raw products from which something is made ***or*** apparatuses necessary to make something.

Like the Director in *E & B Granite*, the Director here urges for a singular definition of materials, limited only to raw products. But this Court has never limited "materials" solely to raw ingredients, and it should not do so now.

If the term "materials" in section 144.054.2 were limited to raw materials used to make another product, the legislature would have used that term as it did twice in another subsection of section 144.030: "… exclusive of the cost of electrical energy so used or if the ***raw materials*** used in such processing contain at least twenty-five percent recovered materials as defined in section 260.200. There shall be a rebuttable presumption that the ***raw materials*** used in the primary manufacture of automobiles contain at least twenty-five percent recovered materials." § 144.030(12), RSMo (emphasis added).

Had the legislature intended "materials" in section 144.054.2 to only mean raw materials, it could have said so when it enacted that exemption years after section 144.030. "The legislature's use of different terms in the same statute is presumed to be intentional." *Alberici Constructors, Inc. v. Dir. of Revenue*, 454 S.W.3d 632, 638 (Mo. banc 2015). This Court "cannot simply insert terms that the legislature has omitted." *Loren Cook Co. v. Dir. of Revenue*, 414 S.W.3d 451, 454 (Mo. banc 2013).

The legislature knew how to differentiate the term "raw materials" from "materials" in Chapter 144 and chose not to do so in section 144.054.2. Thus, the legislature must have intended "materials" to have a broader meaning.

Notably, the Director's own regulations interpret the term "materials" as items other than raw ingredients: sandpaper used to make wooden horses, soap to wash automobiles, crop cards used to hold individual negatives (and discarded after a single use), and the tape used to connect negative strips, are all considered by the Director as "materials used or consumed" in making a product under section 144.054.2. 12 CSR 10-110.201(3); 12 CSR 10-111.011(4)(B); App 45, 48. Sandpaper, soap, tape, and crop cards are not raw ingredients, but are exempt "materials" under the Director's interpretation of section 144.054.2.

The only argument the Director gives for why these items differ from the Center's items is that the regulation's items, which are "used up in washing or processing a finished product differ from an apparatus on which a product is made." Res.Br. at 40. But if the Director seeks to limit "materials" under section 144.054.2 to raw ingredients,

sandpaper, soap, tape, and crop cards do not qualify. Yet, under the Director's own interpretation of the statute, they are exempt as "materials."

Further, the Director's argument that section 144.054.2's exemption does not exempt needles, cannulas, filter, or syringes because they are not raw ingredients used to make a product contradicts its own Letter Ruling 7873 from September 2017, which held that these exact types of items are exempt under section 144.054.2: "Are Applicant's purchases of weigh boats/papers, sterile tubing sets, sterile syringes, needles, and various sized filter bags exempt from state sales tax and state and local use tax, but not local sales tax, under Section 144.054, RSMo? Yes." App 42.

The term "materials" under section 144.054.2 is not limited to raw materials. The items the Center uses to compound drugs are consistent with other items the Director has exempted as "materials" under section 144.054.2. The Commission's decision should be reversed.

II. The Commission was correct that the compounded drugs are products.

The Director's argument that a "product" under section 144.054.2 must be "sold" for final use or consumption is undercut by the absence of any language in section 144.054.2 limiting its application to products intended to be sold. While the exemptions in sections 144.030.2(2)-(5) exempt products "intended to be sold ultimately for final use or consumption," section 144.054.2 omits this language, instead exempting "any product."

Because section 144.054.2 was passed after section 144.030(2)-(5), the legislature must not have intended to limit the resulting products in section 144.054.2 to those

intended to be sold for final use or consumption. Indeed, while the Director cites to the *DST* case in support, the taxpayer in *DST* sought an exemption under section 144.030.2(5), not section 144.054.2. *DST Sys., Inc. v. Dir. of Revenue*, 43 S.W.3d 799, 800 (Mo. banc 2001). Thus, the Center's compounded drugs do not need to be "sold" for them to qualify as products under section 144.054.2.

The Commission was correct that the Center's compounded drugs are products. "To prove that a particular good or service constitutes a 'product,' the taxpayer does not have to actually market the product, but it is incumbent on the taxpayer to prove the existence of a market, whether or not the product is actually marketed by the taxpayer." *Fenix Construction Comp. of St. Louis v. Dir. of Revenue*, 449 S.W.3d 778, 780 (Mo. banc 2014) (internal quotation omitted).

The Center's owner, Dr. Padda, testified that his compounded drugs involve around 18 common formulas based on diseases and joints in the body. Tr. at 45-46. The specific recipe is not based on the particular patient, but rather on the disease or joint pain any prospective patient may be suffering from. LF at 67; Tr. 45-46. A good or a service "qualifies as a product only if it can be marketed to various buyers." *Fenix*, 449 S.W.3d at 780. Based on the record, the Commission was correct in finding that the Center's compounded drugs are marketable to various patients and are products under section 144.054.2. Unlike *Fenix*, where the testimony demonstrated that each wall was designed for a particular building and could not be sold to any other person, the Center's compounded drugs could be used by hundreds of different patients who are suffering from the same disease or joint pain. *See id.* at 780-781.

The Director also makes the incorrect assumption that, because the Center's service of providing these pain treatments to patients is nontaxable, the compounded drugs cannot be a product. Res.Br. at 36-37. The Director's argument primarily relies on *International Business Machines Corp. v. Director of Revenue*, 958 S.W.2d 554 (Mo. banc 1997), where this Court, again, was not interpreting section 144.054.2, but section 144.030.2(5).

Quoting *International Business Machines*, the Director argues that "this exemption applies '***to machinery and equipment that generate sales of tangible personal property or taxable services***.'" Res.Br. at 36-37 (emphasis added). The preceding half of that quote, however, demonstrates that the Court's reasoning behind this holding is entirely dependent on the language of section 144.030.2(5): "***By use of the term 'sold' in section 144.030.2(5)***, the General Assembly intended that exemption to apply to machinery and equipment that generate sales of tangible personal property or taxable services." *Int'l Bus. Machines*, 958 S.W.2d at 557-558 (emphasis added); Res.Br. at 36-37.

While section 144.030.2(5) limits exempted products to only those "intended to be ***sold*** ultimately for final use or consumption," section 144.054.2 contains no such limitation. The word "sold" does not appear anywhere in section 144.054. In omitting that term (or any other limiting language) the legislature intended the phrase "any product" in section 144.054.2 to apply to a broader subset of items, not solely those intended to be sold ultimately for final consumption (i.e. those that would generate a taxable service).

This Court implied as much in *International Business Machines*, noting that section 144.030.2(5) does not exempt "any product" (as section 144.054.2 does), but only those products intended to be sold for final use or consumption: "Section 144.030.2(5), however, does not exempt sales of machinery and equipment used directly to manufacture *any* product. The statute does not end with the word 'product.' Rather, section 144.030.2(5) exempts sales of machinery and equipment used directly to manufacture a product 'which is intended to be sold ultimately for final use or consumption.'" *Int'l Bus. Machines*, 958 S.W.2d at 557 (emphasis in original).

Section 144.054.2 does exempt "any product," and ends there. The Director's reliance on *International Business Machines* is misplaced.

It makes sense that section 144.054.2 would not limit exempted products to only those that would generate a taxable service because, in the medical field, items that fall squarely within section 144.054.2's exemption may never be taxed due to exemptions in unrelated tax statutes. App 41. For example, the Director's Letter Ruling 7873 acknowledged that the applicant who sold compounded medication to hospitals was exempt from sales tax on those sales under a different exemption in section 144.030. *Id*. Likewise, under the Director's argument, taxes would also not be collected when the hospital physicians or nurses administer those compounded medications because those are exempted medical services. *See* Res.Br. at 36. Nonetheless, the Director found in the Letter Ruling that the items used by the applicant to compound medication are exempt under section 144.054.2 because the applicant "engaged in compounding various drug components into medications, which are new products, used in hospitals and surgical

centers." App 42. Like the Center's compounded medication, the medications compounded in the Director's Letter Ruling are never taxed, yet the Director does consider the items exempt under section 144.054.2.

The Director's argument that an industrial compounding operation that sells drugs to hospitals is somehow different than a clinic that compounds drugs to then provide to patients is unsupported. The Director bases the argument—as is the theme throughout this section—on the fact that an industrial compounding operation ***sells*** compounded drugs. But this argument is negated by the lack of any language in section 144.054.2 requiring the resulting products to be sold, and the presence of "sold" in various subsections of section 144.030.2.

The Commission was correct that the compounded drugs are "products" under section 144.054.2.

III. The exemption is not limited to industrial activity.

Had the legislature intended the exemption in section 144.054.2 to apply only to industrial activities, it would not have reinstated the *DST* and *Bell* cases, which held that materials or equipment used in the transmission of a human voice over a telephone line or the organization of information through computer technology are exempt from use tax under the manufacturing exemption. The Director is correct that the 2018 amendment did not overturn this Court's line of cases noting the industrial connotation of section 144.054.2—nor does the Center argue so in its brief—but if this Court's objective is to decipher the intent of the legislature, the legislature's revival of the *DST* and *Bell* cases by specifically mentioning those cases in the amended text of section 144.054.2

demonstrates its intent that section 144.054.2 may apply to activities outside of the traditional industrial context.

Contrary to the Director's contention, the Center never argued in its initial brief that the 2018 legislative amendment abrogated any other cases except *IBM*. Res.Br. at 50-51; App.Br. at 17. But as the legislative intent of section 144.054.2 evolves and becomes clearer, so too should this Court's interpretation of the statute.

Further, the purpose behind this Court's holdings recognizing the industrial nature behind section 144.054.2 is important. In *Aquila*, the first case where this Court applied an industrial connotation to section 144.054.2, the Court rejected a taxpayer's attempt to fit the preparation of food into the "processing" exemption where that activity was plainly not processing. *Aquila Foreign Qualifications Corp. v. Dir. of Revenue*, 362 S.W.3d 1, 5 (Mo. banc 2012). The Court held that section 144.054.2 contains industrial terms and that the legislature did not intend to include food preparation in the term "processing" when the legislature could have used terms such as "preparing" or "serving" food instead. *Id*. Likewise, in *Fred Weber*, the taxpayer sought to fit the activity of paving roads into the "manufacturing" exemption, but the Court noted, that given the industrial terms of section 144.054.2, the paving companies were not manufacturing roads, but constructing them. *Fred Weber, Inc. v. Dir. of Revenue*, 452 S.W.3d 628, 631 (Mo. banc 2015). Had the legislature intended to exempt this type of activity, the Court held, it could have used words associated with construction as it had in other sections of the tax code. *Id*.

What distinguishes the Center's activities here from the taxpayers in other cases is that the activity it engages in—the compounding of medication—falls squarely within the common meaning of compounding. Whereas this Court has held that one does not speak of a grocery store bakery as "processing" baked goods, even the FDA speaks of the mixing of medication to create new drugs as "compounding." *See Union Elec. Co. v. Dir. of Revenue*, 425 S.W.3d 118, 124 (Mo. banc 2014). And the Director's Letter Ruling 7873 acknowledged as much, ruling that the applicant's compounding of pharmaceuticals for distribution to hospitals is "compounding" under section 144.054.2. App 41-42.

This Court's cases noting the industrial nature of section 144.054.2 did so in defining what activities qualify under certain terms of section 144.054.2—e.g. that cooking, baking, or serving food is not "processing" and paving roads is not "manufacturing." But absent from any of these cases is a holding by this Court that two taxpayers engaging in the same activity are treated differently simply because of the size of their operations. Where taxpayers engage in the same activity, the exemption should apply the same to small business owners as it does to larger companies.

The only difference between the Center and the applicant in the Director's Letter Ruling is the scale of the operation, not the activity. In both, the compounded drugs are sold—either to tax-exempt hospitals or through tax-exempt medical services to patients. But the activity they engage in is the same: compounding pharmaceuticals to create new drugs.

IV. The case should be remanded for further proceedings.

The Commission's refusal to make a finding of fact should not preclude this Court from addressing the merits of this appeal. The Center's initial brief did not request solely a reversal of the Commission's decision. Instead, it argued that, if this Court should determine that the Center's activities fall under section 144.054.2, the Commission's decision should be reversed and remanded. App.Br. at 14, 26.

After addressing whether the Center's activities fell within the use tax exemption—and determining that they did not—the Commission ended with one paragraph stating that because it could not discern what percentage of items the Center used for compounding products, it did not make a finding of fact on that issue. LF at 77. The Commission did not state that it was refusing to apply the use tax exemption for this reason, only holding that it was refusing to make a finding of fact. Further, earlier in the decision, the Commission found that although all of these items were categorized differently, they "are all used in the process to withdraw, transport, or inject medications," and they "permit the safe mixing and/or administration of medicine because they are sterile." LF at 71.

Accordingly, given its proximity in the decision, it is unclear whether this refusal of the Commission to make a finding of fact was based on its interpretation (or misinterpretation) of the exemption. The Center requests that if this Court determines that the Center's activities qualify for a use tax exemption under section 144.054.2, it remand the case to the Commission for it to clarify its decision or make a finding of fact

on the issue of what percentage of the items are used for compounding based on this Court's interpretation of the exemption.

Alternatively, even if this Court determines that remand is inappropriate, the Court still should interpret the scope of the use tax exemption under section 144.054.2 for the first time since 2016 and the 2018 legislative amendment. Considering the likelihood of recurrence before the Commission, the Director, and this Court, the precedent the decision will carry for subsequent cases before the Commission, and this Court's role as the final interpreter of Missouri's tax statutes, the Court should address whether the Center's activities fall within the use tax exemption under section 144.054.2.

CONCLUSION

For the reasons stated above and in the Center's initial brief, the Center requests the Court reverse the decision of the Commission and remand for further proceedings.

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CERTIFICATE OF COMPLIANCE

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/s/ *Paul L. Brusati*