

IN THE SUPREME COURT OF MISSOURI

No. SC99367

CARFAX, INC., Respondent,

v.

DIRECTOR OF REVENUE, STATE OF MISSOURI, Appellant.

APPEAL FROM THE ADMINISTRATIVE HEARING COMMISSION

NO. 18-1587

THE HONORABLE RENEE T. SLUSHER, COMMISSIONER

BRIEF OF RESPONDENT

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INTRODUCTION

Each month, Carfax, Inc. (“Carfax”), collects over 1.3 billion records containing information about used vehicles from approximately 112,000 different sources. Through automated processes that involve the machinery and equipment at issue in this case, Carfax uses this massive amount of raw data to create concise vehicle history reports (VHRs) about individual vehicles, which it sells to consumers and car dealers. VHRs are available for approximately 785 million used cars and light trucks.

Contrary to the Director’s assertions, Carfax does not merely “translate and transmit” raw data to its customers: its processes are significantly more complex. Before the data collected by Carfax can be included in VHRs, it must be not only be organized, but corrected, interpreted, verified, and matched with the vehicle identification number (VIN) of the correct vehicle. The VHRs include much more than just the information from this raw data, but also Carfax’s own insight and analysis, as well as graphic design and artwork.

As the Administrative Hearing Commission (“Commission”) correctly ruled in this case, this process of creating VHRs meets this Court’s definition of “manufacturing” as adopted and applied in the context of the sales and use tax exemption statutes. Carfax’s production of VHRs encompasses “the organization and creation of intangible products such as computer data” which this Court has stated “*can* constitute manufacturing” provided the processes at issue create an intangible product through “the alteration or physical change of an object or material in such a way that produces an article with a use, identity, and value different from the use, identity and value of the original.” *IBM Corp. v. Director of Revenue*, 491 S.W.3d 535, 536-537 (Mo. banc 2016), *quoting Galamet, Inc. v.*

Director of Revenue, 915 S.W.2d 331, 333 (Mo. banc 1996). The VHRs are a product with a use, identity, and value that is completely different from that of the original disorganized raw data. Additionally, the Commission’s finding of manufacturing is supported by this Court’s ruling in *DST Systems, Inc. v. Director of Revenue*, 43 S.W.3d 799 (Mo. banc 2001), which was expressly affirmed by the legislature in its recent amendments to §§ 144.030.2(5) and 144.054.2, RSMo.¹

Further, the Commission also correctly ruled that VHRs are products “intended to be sold ultimately for final use or consumption” within the meaning of §§ 144.030.2(5), as defined by § 144.010.1(9), RSMo.² Section 144.010.1(9) plainly provides that services subject to sales or use taxes in other states meet this definition. Here, the evidence presented by Carfax, as well as the statutes of other states, establish that VHRs are a “service that is subject to sales or use tax . . . in other state[s].” The Commission’s ruling on this issue is supported by competent and substantial evidence and authorized by law and should therefore be upheld by the Court.

¹ As noted in the Commission’s decision, during the tax periods at issue in this case, the exemption currently found in § 144.030.2(5) was numbered § 144.030.2(6) and published in RSMo Supp. 2013, 2014, 2015, and 2016. Subsequent to the tax periods at issue, this subdivision was renumbered (5) and amended by S.B. 768 (2018). L.F. 49, n. 12; App. 115. To minimize confusion, this exemption is referred to as § 144.030.2(5), throughout this brief. Section 144.054.2 was also published in RSMo Supp. 2013, 2014, 2015, and 2016 during the tax periods at issue in this case, and amended by S.B. 768 (2018). All other statutory citations are to the Revised Statutes of Missouri (“RSMo”) 2016, as amended, unless otherwise noted.

² Section 144.010.1(9) has also been renumbered since the tax periods at issue in this case. Previously, it was numbered § 144.010.1(15) and published in RSMo Supp. 2013. This subdivision was renumbered (9) effective October 2016. L.F. 49, n. 13; App. 115. For clarity, this provision is referred to as § 144.010.1(9) throughout this brief.

STATEMENT OF FACTS

The Commission conducted a hearing in this case, during which Carfax presented detailed evidence concerning its processes and products and the machinery and equipment for which it claimed exemptions from sales and use tax. This evidence was generally not contested or controverted by the Director, and the facts of this case are not in dispute. Because Carfax finds the Director's statement of facts to be incomplete, Carfax submits the following statement of facts. Mo. S. Ct. Rule 84.04(f).

The transactions at issue in this case are purchases made by Carfax from October 1, 2013 through September 30, 2016. *See* Pet. Ex. 9; Resp. Ex. A. Tax was assessed by the Director on these transactions for the quarterly tax periods ending December 31, 2013 through September 30, 2016. L.F. 45; App. 111. These are the relevant tax periods in this case (the "Tax Periods").

Vehicle History Reports

Carfax is in the business of creating vehicle history reports ("VHRs"), which it sells to consumers and car dealers. L.F. 41; App. 107; Tr. 26, 28. VHRs are available from Carfax for each of the 785 million cars and light trucks sold in the United States and Canada since 1981. L.F. 41; App. 107; Tr. 27-28. A VHR provides information about a specific vehicle in a succinct, easy to understand standard format with artwork and graphic design—including the company's trademark cartoon fox, the "Carfox"—that highlights important information. Petitioner's Exhibits 1, 2 and 3 are examples of VHRs from the Tax Periods. Pet. Ex. 1, 2, and 3; App. 1.

Generally, customers buy VHRs to check the history of a vehicle, which includes where it has been, what has happened to it, and how it has been used. Tr. 29. The information on a VHR includes the ownership history and title history of a vehicle, a listing of any accidents or issues related to the vehicle, and a “detailed history” that includes the date and source of any pertinent information provided to Carfax about the vehicle, along with the vehicle mileage associated with each listed event. Pet. Ex. 1, 2 and 3 at 1-5; App. 1, 6, 12. This includes a description of maintenance and repairs performed on the vehicle, information concerning the vehicle’s ownership and registration, and manufacturer recall notices, among other things. Pet. Ex. 1, 2 and 3 at 2-5; App. 2, 7, 13.

In addition to the specific facts listed in the detailed history of a vehicle, the VHRs include Carfax’s own insight and opinions about the vehicle. Tr. 49. For example, Carfax can evaluate a vehicle’s maintenance record based on the company’s knowledge of the recommended maintenance for all vehicles to determine whether the vehicle has received all the recommended oil changes. Tr. 50. If so, the VHR will prominently state that the vehicle has been “well maintained.” Tr. 50; Pet. Ex. 3 at 1; App. 12. During the Tax Periods, the VHRs produced by Carfax also included a “Price Calculator” that indicated how the price of the vehicle in question should compare to the vehicle’s “retail book value” from a standard pricing guide website, such as Kelley Blue Book or Edmunds. L.F. 42; App. 108; Tr. 50-51; Pet. Ex. 1, 2 and 3 at 1; App. 1. The VHRs currently provide history-based pricing, showing the reasonable retail or wholesale price of the vehicle based on its history. Tr. 50.

The VHRs also provide Carfax's analysis of issues related to a vehicle, such as whether the vehicle was driven less than the industry average number of miles each year. Tr. 51; Pet. Ex. 3 at 3; App. 14. The VHRs may include Carfax's explanation of title information that may be confusing to a consumer, such as why a vehicle would be titled in one state and registered in another—a common practice with leased vehicles. Tr. 52-53; Pet. Ex. 3 at 3; App. 12.

Another example of Carfax's insight relates to natural disasters such as Hurricane Katrina. Based on the information it collects, Carfax was able to identify vehicles that were located in areas where flooding occurred as a result of this hurricane. This information was included on VHRs for the vehicles identified by Carfax to advise consumers to inspect the vehicles for flood damage. L.F. 42; App. 108; Tr 53-54.

Creating Vehicle History Reports

The process of creating VHRs begins with collecting enormous amounts of raw data from a wide variety of sources. Tr. 31, 33. These sources include state departments of motor vehicles ("DMVs"), equipment manufacturers, car dealers (both from their sales and servicing centers), after-market service shops, insurance companies, vehicle repair centers, auctions, inspections sites, and a number of other locations that have dealt with an automobile. Tr. 43.

The records received are voluminous, with Carfax receiving nearly 1.3 billion records each month. Tr. 43-44. Currently, Carfax receives raw data from approximately 112,000 sources. The raw data are delivered to Carfax electronically. Tr. 47. In their original form, the raw data received by Carfax are not useful to a consumer. Tr. 33, 36, 39-

40; Pet. Ex. 4 at 1; App. 17; Pet. Ex. 5 at 1; App. 20; Pet. Ex. 6 at 2; App. 24. There are a number of reasons this data is not useful to consumers—it may be inaccurate, incomplete, or in a format that is incomprehensible to the ordinary person. In addition, the huge amount of data collected by Carfax simply cannot be processed on an ordinary personal computer, but requires the specialized software and hardware utilized by Carfax in order to be useful. Tr. 40, 43.

The raw data received by Carfax must be transformed through verification, interpretation, merging with other data, and reformatting before it can be included in a VHR. Carfax's transformation and organization of the data is accomplished through automated processes using expensive and sophisticated equipment. Tr. 35, 40, 56-57. The process of transforming and organizing raw data requires the use of machinery and equipment, including servers, software, SAN, power, network, and a variety of other pieces of equipment. L.F. 46-47; App. 112; Tr. 42, 56-57. The equipment is large—significantly larger than a personal computer setup. Tr. 40, 43. The process occurs at Carfax's facility in Columbia, Missouri and principally in a server room approximately 600 square feet in size with about six rows of equipment. Tr. 40, 42, 56-57, 72-73; Pet. Ex. 7; App. 25. The room varies in temperature, hot in some places and colder in others; it has uninterruptible power supplies and “tons of wiring.” Tr. 42.

Upon receipt of the raw data, Carfax first backs up the data and performs a data cleansing process whereby data quality and format is reviewed and organized such that only valuable information is used. L.F. 43; App. 109; Tr. 44-45. At this point, Carfax removes incorrectly-formatted dates or inconsistent odometer readings and identifies data

fields which are confusing, non-valuable, or erroneous. Tr. 44-45. The process is extensive and addresses numerous errors and deficiencies. *Id.* The process is performed principally using automated processes with some occasional manual quality control double-checks. Tr. 45. All records are assigned to individual VINs, which ties them to a specific vehicle. L.F. 44; App. 110; Tr. 38, 57.

Second, after performing data cleansing, Carfax performs a series of steps and other automated processes in order to reduce raw records to standardized formats within Carfax's Vehicle History Database ("VHDB"). The process requires receiving data, adding unique identifiers to the data, verifying and validating the data, sorting the data through a data processing document that describes expected layout of the data, and further editing and standardizing data. Tr. 47-48; Pet. Ex. 8; App. 29. In performing these first two steps, Carfax uses "Data Majique," Carfax's proprietary processing rules. Tr. 46-47, 65.

Third, through a transaction control table (TCT) process coupled with Carfax's proprietary "Vinzilla" process, Carfax is able to take data from the VHDB and assemble an individual VHR in response to a customer request. Tr. 48-49, 65; Pet. Ex. 8; App. 29. The process ensures that all information is written and organized accurately for the consumer's use. Tr. 48-49; Pet. Ex. 8; App. 29.

The following is an example of information concerning an accident as it appears on a VHR, after the raw data provided to Carfax has been transformed by these processes. Note that if a VHR containing this report had been purchased from Carfax during the Tax Periods, all of the text at the top of the report would have been included, but the "severity scale" and damage location diagram would not have appeared on the VHR since these

particular features were added by Carfax later. Tr. 31. All of these features would, however, appear on a VHR for this particular vehicle today:



Tr. 31; Pet. Ex. 4; App. 17.

The raw data Carfax used to create this entry were obtained from four separate records and three different sources. The first record came from a DMV. It included a license plate (the first seven numbers and letters) and report number (the remaining numbers):

6HVC37192453013405

Since this record did not include a Vehicle Identification Number (VIN), Carfax used its automated processes applying multiple business rules to find and validate the VIN that matched this license plate within Carfax's internal databases. Pet. Ex. 4 at 1; App. 17. VINs are unique identifying numbers assigned to a vehicle by a manufacturer at the time a vehicle is produced. Tr. 38.

The state police provided two of the records used for this report: (1) a “Collision File” with information concerning the date, location, cause, and other information about the accident, and (2) a “Party File” with information specific to the vehicle involved such as safety equipment and vehicle occupant information. Pet. Ex. 4 at 1; App. 17. In its raw form, the Collision File looked like this:

"6772528",2014,20150817,"9245",20141230,2230,"13405","", "2", "3", "9", "0900", "0", "1", "2", "", "1", "160",
 ", "RT 50", "36 MILE STONE", "500", "E", "N", "A", "-", "Y", "", "", "", "", "", "", "", "Y", "0", "0", "0", **1**, "A", "-",
 ", "08", 22107, "", "N", "E", "**1**", "A", "A", "H", "-", "D", "D", "0", "", "", "", "", "", "Y", "", "A", "07", "0", "0", "0", "0", "0", "0", "0", "0", "-", "-", "",

Pet. Ex. 4 at 1; App. 17; Tr. 31. The “Party File” as received in its original format appeared as follows:

"6772528",1,"1","Y","M",23,"A","-","W","L","G","Y","-","3","-","-","-","-","-","L","-","0,0","R",2006,"BMW","A","07","-","-","W","-","-","-","-"

Pet. Ex. 4 at 1; App. 17; Tr. 31.

In addition to being in a format that could not easily be understood by a consumer, neither record from the state police included a VIN or license plate number. Pet. Ex. 4 at 2; App. 18; Tr. 32. Carfax had to determine the VIN through a process that correlated the information from these two files with the DMV record, which was tied to a VIN by Carfax through the process described above. *Id.*

A fourth record was received from a towing company. This record included a VIN and appeared as follows in its original format (some information has been redacted by Carfax for proprietary reasons):

"5UXFB53506LV26708","2014-12-30","Accident","[REDACTED]","[REDACTED]","[REDACTED]","[REDACTED]","2006","X6","","","UNKNOWN"

Pet. Ex. 4 at 2; App. 18.

All four of these records are re-written into standardized descriptive text, with additional insight (“minor damage”) computed by Carfax’s proprietary “Vinzilla” processes. The text as it appears on the VHR is:

- **Accident reported: minor damage**
 - **It hit a stationary object**
 - **Damage to front**
 - **Damage to right front**
 - **Airbag deployed**
 - **Vehicle towed**

Pet. Ex. 4 at 2; App. 18. Additional information about this accident, not appearing on the VHR, is retained in Carfax’s Vehicle History Database (VHDB). *See* Pet. Ex. 4 at 3; App. 19.

As this example demonstrates, Carfax is able to take incomplete, variable data that are of no use to the ordinary consumer and, through a process of transformation and organization, create a succinct VHR with information readily usable by the end-consumer. The VHRs created by Carfax inform consumers about whether a vehicle was properly maintained, how its history should affect its fair market value, whether it was leased, and even whether it may have been subject to a natural disaster. Tr. 50-54.

The Sale of VHRs Is Subject to Sales and Use Tax in Other States

During the Tax Periods, the price of an individual VHR was \$39.99. L.F. 41; App. 107; Tr. 28-29; Pet. Ex. 1, 2 and 3 at 1; App. 1. Carfax also offers a subscription service to car dealers that allows the dealers to acquire unlimited VHRs within a specific period of time for a single price. L.F. 41; App. 107; Tr. 64.

VHRs are delivered to Carfax's customers electronically, though the Carfax.com website or via the website of a car dealer. Customers take ownership of the VHRs; they may print out copies, and the VHRs are theirs to keep. Tr. 57-58. The VHRs are formatted for printing, but they may also be viewed online in electronic form. Tr. 57.

Sales of VHRs in Missouri are not subject to sales tax, however, Carfax collected and remitted sales or use tax on its VHR sales in Connecticut, District of Columbia, Hawaii, New Mexico, New Jersey, New York, Ohio, South Carolina, South Dakota, Texas, Washington, and West Virginia during the Tax Periods. L.F. 41; App. 107; Tr. 107-108. Carfax consulted with accountants at the firm PwC to determine which states impose tax on its sales of VHRs. Tr. 108-109. During the Tax Periods, VHRs were the only product or service sold by Carfax subject to sales or use tax in these states. Tr. 109.

Carfax's sales and use tax filings are made through a third-party, Vertex, using information provided and verified by the Carfax accounting team. Tr. 110. Petitioner's Exhibit 13 includes copies of Carfax's sales and use tax returns for the period April 2015 for the states of New York, New Jersey, Texas, Washington, South Carolina and Ohio. Pet. Ex. 13; App. 30. The returns reported sales and use tax collected and remitted by Carfax on its sales of VHRs in each of these states. Tr. 110-113; Pet. Ex. 13; App. 30.

At the hearing before the Commission, Carfax moved the Commission to take official notice of Texas Tax Code §§ 151.0101(a)(12) and 151.0035, the statutes that impose sales and use tax on the sale of VHRs to customers in Texas. Tr. 7. The Director had no objection, and stated on the record that the Commission could take notice of any state statutes without the need for a motion by Carfax. Tr. 8.

The Assessment and Disputed Items

Carfax was subject to an audit by the Department of Revenue for the Tax Periods. Tr. 92. Following the audit, the Director's auditor produced audit work papers which listed specific purchases for which the auditor believed Carfax improperly claimed a sales or use tax exemption. Tr. 93; Resp. Ex. A. On October 26, 2018, the Director issued assessments to Carfax based on the purchases identified as taxable in the audit work papers. Tr. 94; Pet. Ex. 10. The assessments included sales and use tax, interest, and additions to tax (penalties) totalling \$106,161.56.

All of the disputed transactions³ included in the audit and assessments involve purchases of fixed assets by Carfax. L.F. 45-46; App. 111. Fixed assets are items that have a useful life of more than a year, and are typically capitalized for accounting purposes. Tr. 94. The disputed items may be broadly categorized by the type of equipment purchases, namely: network equipment, server equipment, software, SAN – hard drives, conferencing equipment, power-UPS equipment, and miscellaneous items. Tr. 72, Pet. Ex. 9. All of the fixed assets included in the disputed transactions are machinery or equipment used in manufacturing VHRs by Carfax and purchased for the purpose of expanding Carfax's VHR manufacturing processes. L.F. 45-46; App. 111; Tr. 70, 84-85, 95-96. In addition, the

³ Carfax did not dispute certain of the assessed purchases. Tr. 94. Specifically, Carfax agreed that it owed tax on the purchases of expensed items, the tax on which was determined by the auditor through a sampling of Carfax's purchases. Tr. 94. The tax assessed on these items was \$106.88. L.F. 45; App. 111; Tr. 94. The assessment also included use tax on Carfax's purchase of an inflatable "Carfox" which Carfax agreed was a taxable purchase. L.F. 45; App. 111; Tr. 94; Resp. Ex. A at 50.

Commission found that all of the disputed items, except the conferencing equipment were used “directly” in manufacturing. Consequently, the Commission ruled that the conferencing equipment was not exempt under § 144.030.2(5), but was nevertheless exempt under § 144.054.2. L.F. 46, 61; App. 112, 127. The categories of fixed assets at issue in this case include the following:

- Network equipment - equipment involved in the process of computer-to-computer or, more generally, device-to-device communication. Tr. 74-76.
- Server equipment - pieces of electronic equipment that have central processing units (“CPUs”), hard drives, and memory and that execute programs or functions that Carfax uses in its processes. Tr. 73.
- Software - a broad term used to describe programs or applications that run on servers to produce a task. Software is delivered to Carfax electronically. Tr. 82.
- SAN - stands for storage area network and is essentially a large number of drives storing electronic information. Tr. 76.
- Conferencing equipment - equipment used for communication between individuals and groups, and is used in the process of creating VHRs, repairing and troubleshooting problems in Carfax’s processes, and according to Carfax’s Director of Data Center Operations “just about everything we do at Carfax.” Tr. 77-81.
- Power-UPS equipment - used to ensure power coming into server room is consistent. Tr. 83.

- Miscellaneous items - workstation equipment and server cooling equipment.

Workstation is a term classifying the piece of equipment that Carfax's developers use when developing code to run Carfax's automated processes. L.F. 47; App. 113; Tr. 84. Server cooling equipment is used to move air so as to keep equipment from overheating. Tr. 83-84.

Carfax consulted with tax professionals concerning whether it should claim a manufacturing exemption from sales tax on its purchases of computer hardware and software. These professionals included the accounting firm of Pricewaterhouse Coopers and Ed Downey at the law firm Bryan Cave LLP (now Bryan Cave Leighton Paisner LLP). Tr. 115-116.

Previous Assessment Dispute

Carfax was previously audited by the Director for the period July 1, 2009 to June 30, 2012. This audit involved the same issue as this case, namely, whether Carfax's purchases of machinery and equipment purchased to produce VHRs were exempt from sales and use tax under the manufacturing exemptions. Tr. 116. The assessment resulting from this prior audit was issued in June 2014. Tr. 116-117. The assessment was appealed and resolved by settlement on October 31, 2016. Tr. 121; *Petitioner's Motion for Dismissal, Carfax, Inc. v. Director of Revenue*, Missouri Administrative Hearing Commission Case Number 14-1161RV (filed October 31, 2016).

While the prior audit was on appeal, Carfax continued to claim exemptions under §§ 144.030.2(4) and (5) and 144.054 based on consultations with legal counsel and tax

professionals. Tr. 115-116. The purchases at issue in this case all pre-date the October 31, 2016 resolution of the prior audit.

Carfax's Appeal and the Commission's Decision

Carfax filed a timely appeal of the Director's assessments with the Commission. The Commission held a hearing in the case on January 25, 2021 with the Honorable Renee T. Slusher, Commissioner, presiding. The Commission issued its decision on September 30, 2021, and ruled that Carfax was entitled to exemptions under §§ 144.030.2(5) and 144.054.2:

Carfax's purchases of machinery and equipment used to produce its VHRs are exempt from sales and use tax pursuant to § 144.030.2(5), except for the conferencing equipment. The machinery and equipment are also exempt from sales and use tax pursuant to § 144.054.2, including the video conferencing equipment. Carfax owes tax in the amount of \$106.88 on other items purchased.

L.F. 61-62; App. 127.

STANDARD OF REVIEW

The decision of the Commission shall be upheld unless: (1) it is not authorized by law; (2) it is not supported by competent and substantial evidence upon the whole record; (3) a mandatory procedural safeguard is violated; or (4) it is clearly contrary to the Legislature's reasonable expectations. Section 621.193; *Concord Publishing House, Inc. v. Director of Revenue*, 916 S.W.2d 186 (Mo. banc 1996).

This Court's interpretation of Missouri's revenue laws is *de novo*. *Zip Mail Services, Inc. v. Director of Revenue*, 16 S.W.3d 588, 590 (Mo. banc 2000). In *AAA Laundry and Linen Supply Co. v. Director of Revenue*, 425 S.W.3d 126, 128 (Mo. banc 2014), this Court explained its role in reviewing administrative decisions involving sales and use tax exemptions:

When construing sales and use tax exemptions, the Court strives to 'give effect to the General Assembly's intent, using the plain and ordinary meaning of the words.' *Branson Properties USA, L.P. v. Dir. of Revenue*, 110 S.W.3d 824, 825–26 (Mo. banc 2003). An exemption is 'strictly construed against the taxpayer,' however, and 'is allowed only upon clear and unequivocal proof, and doubts are resolved against the party claiming it.' *Id.* at 826. Moreover, the Court does not write on a blank slate in each and every tax case, and *stare decisis* plays as great a role in such cases as it does in every other area of the Court's jurisprudence.

POINTS RELIED ON

- I. **Carfax’s production of Vehicle History Reports (VHRs) constitutes “manufacturing” within the meaning of §§ 144.030.2(5) and 144.054.2. (Response to Appellant’s Point I).**

DST Systems, Inc. v. Director of Revenue, 43 S.W.3d 799 (Mo. banc 2001)

Concord Publishing House, Inc. v. Director of Revenue, 916 S.W.2d 186 (Mo. banc 1996)

Galamet, Inc. v. Director of Revenue, 915 S.W.2d 331, 333 (Mo. banc 1996)

§ 144.030.2(5), RSMo

§ 144.054.2, RSMo

§ 144.010.1(9), RSMo

12 C.S.R. § 10-111.010

- II. **The Commission’s findings that Carfax paid sales and use tax on its sales of VHRs in states other than Missouri and that Carfax was liable for this tax is supported by competent and substantial evidence and authorized by law. (Response to Appellant’s Point II(A)).**

Texas Tax Code § 151.010

Texas Tax Code § 151.0035

New York Tax Law § 1105(c)(1) 46

§ 144.010.1(9), RSMo

- III. **The Director’s interpretation of § 144.010.1(9) is inconsistent with the plain language of the statute, the reasonable expectations of the General Assembly, and the Director’s own regulations. (Response to Appellant’s Point II(B)).**

Jones v. Director of Revenue, 832 S.W.2d 516 (Mo. banc 1992)

12 C.S.R. § 10-111.010

§ 144.010.1(9) RSMo

§ 143.903, RSMo

35 Illinois Compiled Statutes § 120/2

35 Illinois Compiled Statutes §120/2-10

Arizona Revised Statutes § 42-5008,

Arizona Revised Statutes §42-5010

Arizona Revised Statutes §42-5061

ARGUMENT

I. Carfax’s production of Vehicle History Reports (VHRs) constitutes “manufacturing” within the meaning of §§ 144.030.2(5) and 144.054.2.

The Commission correctly concluded that the machinery and equipment purchased and used by Carfax to produce VHRs were exempt from Missouri sales and use tax under §§ 144.030.2(5) and 144.054.2, finding, specifically, that all disputed items were exempt under § 144.054.2 and all disputed items except video conferencing equipment were exempt under § 144.030.2(5). Both sections apply to machinery and equipment used in “manufacturing.”

The record in this case fully supports the Commission’s conclusion that “Carfax alters or physically changes the raw data to ‘produce an article with a use, identity and value different from the use, identity and value of the original.’” L.F. 57; App. 123. Indeed, Carfax collects billions of records with information about vehicles—records that are both inaccessible and unusable to the ordinary consumer—and organizes and transforms them into succinct, meaningful VHRs that are useful and valuable to Carfax’s customers. This is manufacturing.

The Director misunderstands these facts. He has asserted that Carfax is not a manufacturer because “all Carfax does in creating VHRs is organize, translate and transmit data in an intangible form.” App. Br. at 18. The Director’s description is incomplete and too narrow: he asks that this Court look no further than furnishing one data point, ignoring entirely the mass of jumbled, disaggregated data from which Carfax synthesizes user-friendly material. Seeing only a fraction of Carfax’s processes, the Director asserts that

Carfax's processes are merely "translation" and that its output is the exactly same information it receives. App. Br. at 22-23.

For these reasons, the Director's brief misstates the law and inaccurately describes Carfax's processes and its products.

Section 144.030.2(5)

Carfax qualifies for an exemption under § 144.030.2(5). As noted by the Commission, although § 144.030.2 was amended annually from 2013-2016 (*i.e.*, during the Tax Periods), these amendments did not change the wording of the exemption now found in subdivision (5) of § 144.030.2. L.F. 49-51; App. 115. Thus, during the Tax Periods and currently, this subdivision provided and provides an exemption from sales and use tax for: (1) "machinery and equipment" that is (2) "purchased and used to . . . expand existing manufacturing, mining or fabricating plants in the state" (3) "if such machinery and equipment is used directly in manufacturing" (4) "a product which is intended to be sold ultimately for final use or consumption." In turn, the term "product which is intended to be sold ultimately for final use or consumption" is statutorily defined by § 144.010.1(9).

While the elements of § 144.030.2(5) remained unchanged during the Tax Periods, amendments to this subdivision in 2018 underscore Carfax's qualification as a "manufacturer." Specifically, in 2018, the Legislature amended what is now § 144.030.2(5) through SB 768 in response to this Court's decision in *IBM Corp. v. Director of Revenue*, 491 S.W.3d 535 (Mo. banc 2016) ("*IBM*"). This amendment left unchanged the basic elements of the exemption now found in subdivision (5), renumbered the subdivision, and added the language shown in bold text below:

(5) Machinery and equipment, and parts and the materials and supplies solely required for the installation or construction of such machinery and equipment, purchased and used to establish new or to expand existing manufacturing, mining or fabricating plants in the state if such machinery and equipment is used directly in manufacturing, mining or fabricating a product which is intended to be sold ultimately for final use or consumption. **The construction and application of this subdivision as expressed by the Missouri supreme court in *DST Systems, Inc. v. Director of Revenue*, 43 S.W.3d 799 (Mo. banc 2001); *Southwestern Bell Tel. Co. v. Director of Revenue*, 78 S.W.3d 763 (Mo. banc 2002); and *Southwestern Bell Tel. Co. v. Director of Revenue*, 182 S.W.3d 226 (Mo. banc 2005), is hereby affirmed; . . .**

Section 144.010.1(5) (emphasis added). As more fully discussed below, the legislature’s express affirmation of *DST Systems, Inc. v. Director of Revenue* confirms that “organizing information through computer technology is ‘manufacturing.’” *See DST Systems, Inc. v. Director of Revenue*, 43 S.W.3d 799, 802 (Mo. banc 2001), *quoting, Concord Publishing House, Inc. v. Director of Revenue*, 916 S.W.2d 186, 191 (Mo. banc 1996).

The Director’s arguments in this case focus solely on the third and fourth elements required by this statute, namely, whether Carfax uses the items in question in manufacturing a product which is intended to be sold for final use or consumption. There is no dispute that the items at issue are machinery and equipment that were purchased for the expansion of Carfax’s Missouri production facilities. L.F. 51, App. 117.

Section 144.054.2

Carfax’s purchases of machinery and equipment for use in its VHR process also qualify for an exemption under § 144.054.2. Subsection 2 of § 144.054 is like § 144.030.2(5) in that it provides an exemption from sales and use tax for machinery and

equipment used in manufacturing, but unlike § 144.030.2(5), the plain language of § 144.054.2 does not require that the machinery and equipment be used “directly” in manufacturing, nor does it require that the product produced by the taxpayer be “sold ultimately for final use or consumption.”

In *Int’l Bus. Machines v. Director of Revenue*, 958 S.W.2d 554 (Mo. banc 1997) (“*Int’l Bus. Machines*”)⁴ this Court ruled that the term “product” means “an output with a market value” and that a product “can be either tangible personal property or a service.” *Id.* at 557. This definition of “product” has been applied by this Court in the context of § 144.054.2. See *Fenix Construction Co. v. Director of Revenue*, 449 S.W.3d 778, 780 (Mo. banc 2014). This meaning of the term “product” is more encompassing than a “product which is intended to be sold for final use or consumption” found in § 144.030.2(5). The Commission’s ruling that Carfax produces a “product” within the meaning of § 144.054.2 should therefore be upheld even assuming *arguendo* this Court accepts the Director’s assertions (discussed in points II and III, below) that the VHRs are not a “product which is intended to be sold for final use of consumption” within the meaning of § 144.010.1(9). The definition found in § 144.010.1(9) does not apply in the context of § 144.054.2.

The VHRs are “an output with a market value” and therefore a “product” as

⁴ *Int’l Bus. Machines* concerned the application of section § 144.030.2(5) to the same operations and equipment that were at issue in *DST Systems, Inc. v. Director of Revenue*, 43 S.W.3d 799 (Mo. banc 2001) (“*DST*”). *Int’l Bus. Machines* involved a claim for refund of taxes paid by DST on computer equipment and software that DST purchased from International Business Machines Corp. (commonly referred to as IBM). We refer to the 1997 case as “*Int’l Bus. Machines*” and the 2001 case as “*DST*” consistent with the Commission’s references to the two cases.

demonstrated by the fact that during the Tax Periods, Carfax sold individual VHRs for \$39.99 and also sells subscriptions that enable customers to acquire unlimited VHRs for a single price. L.F. 41; App. 107; Tr. 28-29, 64; Pet. Ex. 1, 2 and 3 at 1; App. 1. An individual VHR can be sold to multiple customers interested in the history of the same vehicle. Tr. 59-60. Access to all VHRs through subscriptions can be sold to any used car dealer, or anyone else who frequently buys or sells used cars. There is therefore a market for Carfax's products. The facts of this case are thus distinguishable from *Fenix Construction*, where this Court ruled that "tilt-up concrete wall panels" constructed by the taxpayer were not a "marketable product for purposes of section 144.054." The walls are "constructed on site, can be used only for that particular building, and have not demonstrated actual or potential market value to a buyer other than the building owner." *Id.* at 781. Because the VHRs, unlike the wall panels at issue in *Fenix*, are an "output with a market value," the VHRs are a "product" within the meaning of § 144.054.2, as the Commission correctly ruled. *See* L.F. 60-61; App. 126.

A third difference between the exemptions in § 144.030.2(5) and § 144.054.2 is that during the Tax Periods, § 144.054.2 applied to state sales and use tax, and local use tax, but not local sales tax, while § 144.030.2(5) applies to state and local sales and use tax.

Like § 144.030.2(5), § 144.054.2 was amended by the legislature in 2018 through SB 768 in response to this Court's decision in *IBM Corp. v. Director of Revenue*, 491 S.W.3d 535 (Mo. banc 2016) ("*IBM*"). As with the amendments to § 144.030.2(5), the legislature left unchanged the basic elements of the exemption (in italics and underlined

below), but added language affirming *DST Systems, Inc. v. Director of Revenue*, as shown in bold text below:

2. In addition to all other exemptions granted under this chapter, there is hereby specifically exempted from the provisions of sections 144.010 to 144.525 and 144.600 to 144.761, and from the computation of the tax levied, assessed, or payable under sections 144.010 to 144.525 and 144.600 to 144.761, electrical energy and gas, whether natural, artificial, or propane, water, coal, and energy sources, chemicals, machinery, equipment, and materials used or consumed in the manufacturing, processing, compounding, mining, or producing of any product, or used or consumed in the processing of recovered materials, or used in research and development related to manufacturing, processing, compounding, mining, or producing any product. The exemptions granted in this subsection shall not apply to local sales taxes as defined in section 32.085 and the provisions of this subsection shall be in addition to any state and local sales tax exemption provided in section 144.030. **The construction and application of this subsection as expressed by the Missouri supreme court in *DST Systems, Inc. v. Director of Revenue*, 43 S.W.3d 799 (Mo. banc 2001); *Southwestern Bell Tel. Co. v. Director of Revenue*, 78 S.W.3d 763 (Mo. banc 2002); and *Southwestern Bell Tel. Co. v. Director of Revenue*, 182 S.W.3d 226 (Mo. banc 2005), is hereby affirmed.**

RSMo § 144.054.2 (emphasis added).

Manufacturing

Carfax qualifies as a manufacturer for purposes of §§ 144.030.2(5) and 144.054.2. In *IBM*, this Court stated that “the organization and creation of intangible products such as computer data *can* constitute manufacturing,” ruling, however, that the use of computers to transmit financial information between banks was not “manufacturing.” *IBM*, 491 S.W.3d at 536. As the Court explained:

Products, whether tangible or intangible, still must undergo ‘the alteration or physical change of an object or material in such a way that produces an article with a use, identity, and value different from the use, identity, and value of the original,’ *Galamet, Inc. v. Director of Revenue*, 915 S.W.2d 331, 333 (Mo. banc 1996), to be manufactured.

Id. at 546-537.

The Court’s analysis recognized a distinction between “transformation of a product” and the “mere transmission of information,” noting that the latter is not “manufacturing.” *IBM*, 491 S.W.3d at 540. The Court concluded that the taxpayer in *IBM* was not a manufacturer since it “does not create or transform a product.” *Id.* at 537.

This is not the case with Carfax. Carfax transforms data into a new, useful product. As the Commission recognized, the facts here are not analogous to those at issue in *IBM*. The Commission’s findings explain that, unlike in *IBM*, Carfax changes and adapts raw data that is distinct and apart from the VHRs:

The VHRs are not simply a conduit by which Carfax summarizes raw data that it receives from 112,000 different sources. **The VHRs have a distinct identity and value apart from the raw data used to create them.** . . . VHRs have added value for which customers are willing to pay. Carfax’s customers on their own cannot readily ascertain the information contained in the large volume of raw data that is otherwise cleansed, reviewed for errors or inconsistencies, organized, and summarized by Carfax’s propriety [sic] software. Carfax at times also manually reviews the data for errors and inconsistencies. **Carfax’s process ‘changes and adapts something practically unsuitable for any common use into something suitable for common use.’ 12 CSR 10-111.010(2)(E)(ii).**

L.F. 56; App. 122. (emphasis added). Notably, in rendering its decision, the Commission applied a definition of manufacturing codified by the Director in the Department of

Revenue’s regulations, namely, a “process [that] changes and adapts something practically unsuitable for any common use into something suitable for common use.” *See* 12 CSR 10-111.010(2)(E)(ii); App. 129. This long-established definition has been repeatedly affirmed and applied by this Court. *See, e.g., Galamet, Inc. v. Director of Revenue*, 915 S.W.2d 331, 333 (Mo. banc 1996); *Jackson Excavating Co. v. Admin. Hearing Commission*, 646 S.W.2d 48, 50 (Mo. 1983); and *Heidelberg Central, Inc. v. Director of Department of Revenue*, 476 S.W.2d 502, 504 (Mo. 1972).

Carfax’s Production of VHRs is Manufacturing

Ample evidence supports the Commission’s conclusion that Carfax qualifies for the manufacturing exemptions. At the evidentiary hearing, Carfax introduced into evidence copies of VHRs produced by Carfax during the Tax Periods, representative samples of the types of raw data received by Carfax, flow charts and testimony describing in detail the complex computer processes performed by Carfax to transform the data in order to create VHRs, and testimony describing in detail the machinery and equipment at issue. *See* Pet. Ex. 1, 2, 3, 4, 5, 6, and 8; App. 1; Tr. 25-66, 68-86.

The VHRs are intangible products delivered to Carfax’s customers electronically and are formatted for printing. Petitioner’s Exhibits 1, 2 and 3 are printouts of VHRs. Each VHR is 5 or 6 pages in length. All of the VHRs have a standard layout, format, and appearance. They are designed to be easily understood by the average person and used in evaluating the condition and value of a used car. At the top of the front page, each VHR identifies the vehicle that is the subject of the report. Important information about the vehicle is highlighted through the use of color symbols (*e.g.*, a green box with a check –

no accident / damage reported to Carfax; a blue circle with a number 1 – one owner vehicle). Carfax’s trademark cartoon “Carfox” is also prominently displayed. On Petitioner’s Exhibit 3 the Carfox is pictured holding a gold shield announcing the vehicle was “well maintained” through “regular oil changes.” The highlighted information and graphic art represent Carfax’s analytic and creative input to the VHRs; they are plainly not simply a “translation” of a single record received from a DMV or a car repair shop.

At the center of the first page of the VHRs is the “Carfax Price Calculator,” another example of Carfax’s analytic and creative input to the VHRs. Carfax determines a “price adjustment” to the retail book value of the car, so the customer can easily calculate an adjusted retail value. *See* Pet. Ex. 1, 2, and 3; App. 1. The VHRs explain that this value should be compared to “the seller’s asking price when making your decision.” *Id.* At the bottom of the first page, Carfax provides a summary of the vehicle’s ownership history, including the estimated number of owners, the type of owner, length of ownership, state where the vehicle was owned, estimated miles driven per year, and last reported odometer reading. Again, all of this information represents Carfax’s analysis and synthesis of many separate records. Additional analysis of the title history, actual mileage, accidents, airbag deployment, possible odometer rollbacks, manufacturer recalls, and warranty information is included on page 2 of the VHRs.

The pages that follow set out the vehicle’s “Detailed History.” Each entry in this section of the VHRs includes the date, mileage (if available), source, and a narrative explanation. The detailed histories shown on the sample VHRs include information about each vehicle’s title and registration, safety inspections, repairs and maintenance, and

manufacturer safety recalls. *See* Pet. Ex. 1, 2, and 3; App. 1. As these documents demonstrate, customers who purchase a VHR do not receive a disorganized “data dump,” but instead gain the benefit of Carfax’s extensive knowledge and expertise concerning used car values, which is reflected throughout the reports.

Further, as the Commission correctly notes, the raw data from which the information on the VHRs is created bears no resemblance to these finished reports. Representative samples of raw data received by Carfax are shown on Petitioner’s Exhibits 4 and 6. As set out in detail in the Statement of Facts, Petitioner’s Exhibit 4 demonstrates the many steps taken by Carfax to convert four separate raw data records into information that appears on a VHR. As this example demonstrates, records received by Carfax are in a format that would be nonsensical to an average consumer. Pet. Ex. 4; App. 17; Tr. 33, 36, *see also* Pet. Ex. 6; App. 23; Tr. 38-40 (setting out Carfax’s process for transforming manufacturer’s recall reports). Carfax must transform and organize the raw data to create the VHRs in order to provide information that is useful to consumers, and for which they are willing to pay. Tr. 33, 36, 40. The raw data are often incomplete or inaccurate. Tr. 44-45. Records may include typos, incorrect or fraudulent odometer readings, or may be confusing to the ordinary person. Tr. 44-45. In short, without Carfax’s proprietary processes performed by the machinery and equipment at issue in this case, the data Carfax collects is of no value to the ordinary consumer. Carfax “changes and adapts something practically unsuitable for any common use”—the raw data—into something “suitable for common use,” the VHRs. This is manufacturing. *See Galamet, Inc. v. Director of Revenue*, 915 S.W.2d 331, 333 (Mo. banc 1996).

Additionally, the scope and scale of Carfax's operations support a finding that Carfax is a manufacturer. Carfax processes over 1.3 billion records each month from 112,000 different sources and can produce VHRs for 785 million different vehicles. Tr. 28, 43-44, 47. The equipment used by Carfax in its operations is pictured in Petitioner's Exhibit 7. Pet. Ex. 7; App. 25. As Michael Pierce, Carfax's Director of Dealer Experience explained, this equipment is not like a home computer. Tr. 42-43. A consumer could not process the vast amount of data collected by Carfax with only a personal computer due the enormous volume and complexity of the data. Tr. 40. The scale of Carfax's operations are obviously not comparable to those of a grocery store bakery department or a restaurant kitchen. Accordingly *Union Electric Co. v. Director of Revenue*, 425 S.W.3d 118, 124 (Mo. banc 2014), and *Brinker v. Director of Revenue*, 319 S.W.3d 433, 437-438 (Mo. banc 2010), cited by the Director, are distinguishable from this case. App. Br. at 24.

The Director asserts that Carfax's process of creating VHRs is akin to translating an ancient Greek manuscript into English, and that as such, Carfax is merely "translating" not manufacturing a product. App. Br. at 23-24. This is a gross mischaracterization of the facts of this case. There is no ancient Greek volume of vehicular data that Carfax can pick up, bring home, and translate into a VHR—just scattered pages of smeared text that must be compiled, edited and synthesized before anyone would find them worth reading. As shown in the record, before any records collected by Carfax can be incorporated into a VHR, they must be organized, verified, analyzed, found to be relevant but not redundant, translated into standardized language, and matched to one of the 785 million VINs in Carfax's database. The organized compilation of relevant and accurate information delivered to a

consumer in the form of a VHR does not exist until Carfax produces it, and this finished product bears no resemblance to the disorganized raw data collected by Carfax.

Further, the Director's translation argument ("Information comes in and *the same information goes out*," App. Br. at 22) ignores the law and the significant differences between the VHRs and the raw data. The Director's argument is inconsistent with this Court's newspaper and printed product cases, all of which found manufacturing and all of which could be said to involve the same information on both sides of a process. *See Concord Publishing House, Inc. v. Director of Revenue*, 916 S.W.2d 186 (Mo. banc 1996); and *Heidelberg Central, Inc. v. Director of Department of Revenue*, 476 S.W.2d 502, 506 (Mo. 1972). But even more, while some of the information in a VHR may be the same as the information received in a raw report, it is only through Carfax's processes that this information becomes accessible and comprehensible to a consumer. And without Carfax's added insight and analysis the individual records would be of little value to a consumer attempting to evaluate a used car. As with any manufactured product, a VHR is much more than simply the sum of its individual parts.

In any event, a taxpayer should not be disqualified from claiming the exemptions at issue in this case simply because a word other than "manufacturing" may describe its production process. Although tax exemptions are to be construed strictly against the taxpayer, "that requirement should not nullify the legislative purpose in making the exemption available." *State ex rel. Ozark Lead Co. v. Goldberg*, 610 S.W.2d 954, 957 (Mo. 1981). The manufacturing exemptions would effectively be rendered a nullity if their applicability depends on whether the Director prefers a different word for the process:

nearly every process that alters an object or material to create a new product can be described with a term other than “manufacturing.” Additionally, the application of *stare decisis* should prevent this Court from applying this exemption so narrowly. The following list of production activities is from this Court’s opinion in *Branson Properties USA, L.P. v. Director of Revenue*, 110 S.W.3d 824 (Mo. banc 2003). All of these processes were found by this Court to be “manufacturing,” notwithstanding the fact that all of them are more commonly described using other terms:

- Grinding, crushing, and sorting rock into various sizes for commercial use. *See West Lake Quarry & Material Co. v. Schaffner*, 451 S.W.2d 140, 143 (Mo. 1970).
- Commercial printing. *See Heidelberg Central, Inc. v. Director of Department of Revenue*, 476 S.W.2d 502, 506 (Mo. 1972); *see also Ovid Bell Press v. Director of Revenue*, 45 S.W.3d 880, 884 (Mo. banc 2001).
- Slaughtering livestock to create marketable food. *See Wilson & Co., Inc. v. Department of Revenue*, 531 S.W.2d 752, 754–55 (Mo. 1976); *see also Sipco, Inc. v. Director of Revenue*, 875 S.W.2d 539, 542 (Mo. banc 1994).
- Treating and purifying water. *See Jackson Excavating Co. v. Administrative Hearing Commission*, 646 S.W.2d 48, 51 (Mo. 1983).
- Converting old automobiles/appliances into steel shreds for commercial use. *See Galamet*, 915 S.W.2d at 333–34.

- Manipulating and affixing words onto a page to create a newspaper. *Concord Publishing House, Inc. v. Director of Revenue*, 916 S.W.2d 186, 190 (Mo. banc 1996).

Even plants where cars are manufactured are typically referred to as “vehicle assembly plants” rather than manufacturing plants. In short, as these cases demonstrate, the term “manufacturing” is generic—it applies to many processes that are commonly referred to with more specific terminology. For the manufacturing exemptions to have any application at all, this Court must uphold its precedent that recognizes that these exemptions apply to the alteration or transformation of raw materials to create new products with a use, identity, and value different from the use, identity, and value of the original, *without regard to* whether those processes may also be described by a term other than manufacturing.

DST Systems, Inc.

This Court should also affirm the Commission’s conclusion that the facts of this case are aligned with the facts at issue in *DST Systems, Inc. v. Director of Revenue*, 43 S.W.3d 799 (Mo. banc 2001) (“*DST*”) and support a finding that Carfax is a manufacturer. *See* L.F. at 56; App. 122.

In *DST*, the taxpayer provided services to the mutual fund industry by creating printed materials such as transaction confirmations and quarterly and annual reports to shareholders. *See DST*, 43 S.W.3d at 801. The taxpayer referred to this process as “package production.” *Id.* The process was performed using mainframe computers that ran software applications. *Id.* at 803. The taxpayer used these computers to gather, store, and organize information about shareholders. *Id.* Computer workstations provided the data for the

“packages” and then applications on the mainframes decided what material to place in the “packages” and formatted the shareholder statements. *Id.* This Court held that the mainframe computers, desktop computers, and telephones located at employee workstations were all “used directly in manufacturing” and exempt from tax under § 144.030.2(5). *Id.* at 802-803. In so ruling, this Court re-affirmed its previous holding that “organizing information through computer technology is ‘manufacturing.’” *Id.* at 802, quoting, *Concord Publishing House, Inc. v. Director of Revenue*, 916 S.W.2d 186, 191 (Mo. banc 1996).

Carfax’s processes are analogous to those at issue in *DST*. Carfax creates VHRs for customers using computer systems (servers, network, SAN, etc.) that use complex and meticulously-designed automated processes to run programs, which gather, store, and organize huge amounts of data about vehicles, and ultimately create and format VHRs. Tr. 38-58; Pet. Ex. 8; App. 29.

Carfax’s case differs from *DST* only in that Carfax’s product is sold in electronic form, while *DST*’s processes produced tangible printed materials. Whether *DST* produced a printed product was relevant in both *DST* and the prior case involving *DST Systems, Inc.*’s operations, *Int’l Bus. Machines v. Director of Revenue*, 958 S.W.2d 554 (Mo. banc 1997) (“*Int’l Bus. Machines*”). But the tax periods at issue in both cases pre-dated § 144.010.1(9)’s statutory codification of the definition of “product which is intended to be sold ultimately for final use or consumption” which now expressly provides that a “product” for the purposes § 144.030.2(5) can include tangible personal property *or* a service subject to sales or use tax in a state other than Missouri.

Carfax's operations are equivalent to the material facts that were at issue in *DST*, and this Court's construction and application of the exemption in § 144.030.2(5) in *DST* supports the Commission's conclusion that Carfax, like *DST*, is engaged in manufacturing. As noted above, the legislature expressly affirmed "the construction and application" of § 144.030.2(5) "as expressed by the Missouri supreme court in" *DST*, in its 2018 amendment of this statute. This amendment was in response to this Court's decision in *IBM*, and was apparently added to the statute to clearly signal that *IBM* was not to be construed as overruling *DST*. Applying the "manufacturing" definitions of *DST* gives certainty and meaning to the amendments of SB 768. Therefore, consistent with this legislative intent, the manufacturing exemptions should be interpreted in accord with *DST*, which supports the Commission's conclusions in this case, and cannot be squared with the Director's assertion that Carfax is not a manufacturer.

As demonstrated by the foregoing, the Commission's ruling that Carfax is engaged in manufacturing within the meaning of §§ 144.030.2(5) and 144.054.2, is supported by competent and substantial evidence, authorized by law, and consistent with the reasonable expectations of the General Assembly and should therefore be upheld by this Court.

II. The Commission’s findings that Carfax paid sales and use tax on its sales of VHRs in states other than Missouri and that Carfax was liable for this tax is supported by competent and substantial evidence and authorized by law. (Response to Appellant’s Point II(A)).

The Director argues that the Commission “never found that the VHRs were *subject* to sales and use tax in other states; what it found was that Carfax *collected and paid sales tax* in other states.” App. Br. 36. But the Commission’s decision expressly refutes the Director’s argument:

The VHRs were also “intended to be sold for final use or consumption” because they were “subject to state [sic] or . . . use taxes . . . in [an]other state.” Section 144.010.1(9). While Carfax was not required to collect and pay sales tax in Missouri, it did collect sales and use tax in other states. Carfax established that it collected sales and use tax on the VHRs during the purchase period in states other than Missouri....**Carfax established that it was liable for sales and use tax during the audit period in states other than Missouri.**

L.F. 59-60; App. 125 (emphasis added).

Thus, contrary to the Director’s assertion, *the Commission expressly found that the VHRs were subject to sales or use tax in other states*. Even more, the fact that Carfax paid tax on its sales of VHRs in other states (which the Director agrees Carfax established) is logically consistent with and therefore probative of the fact that the sales were also *subject to tax* in those states. On the other hand, while it may be *possible* that Carfax collected and paid tax it did not owe, this is not likely based on the record in this case.

Carfax presented ample testimony on this issue and introduced into evidence an exhibit demonstrating that VHRs were sold and subject to sales or use tax in other states. In particular, Carfax introduced testimony of Joseph Corr, Senior Director of Tax for IHS

Global, Inc., (Carfax’s parent company), who is an experienced tax professional who oversees Carfax’s sales tax compliance. Tr. 90-91. He holds an MBA in taxation, and has worked in the area of sales and use tax since 1993. *Id.* Mr. Corr expressly and repeatedly testified that Carfax collected and paid sales and use tax on its sales of VHRs:

Q: “[D]id Carfax collect sales or use tax on the sale of vehicle history reports during the audit period at issue in this case?”

A: “Yes.” Tr. 107.

* * *

Q: “In which states does Carfax collect and remit sales or use tax on these sales?”

A: “Currently with several states. The State of Connecticut, District of Columbia, Hawaii, New Mexico, New Jersey, New York, Ohio, South Carolina, South Dakota, Texas, Washington and West Virginia.” Tr. 108.

* * *

Q: “During the tax periods at issue in this case, did Carfax sell anything else that was subject to sales or use tax in those states that you just named?”

A: “No. The vehicle history report has always been the product that has been taxed.” Tr. 109.

* * *

Q: “What is exhibit 13?”

A: “Exhibit 13, some copies of . . . tax returns, sample state that we

provided for the period April 2015, reflecting the returns that were filed by Carfax to the different states.” Tr. 110-111.

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Q: “And were the sales reported on these returns sales of vehicle history reports?”

A: “That is correct, yes.” Tr. 112-113.

Petitioner’s Exhibit 13, referred to in Mr. Corr’s testimony, includes copies of returns clearly titled “sales and use tax return” for the period April 2015 filed by Carfax for the states of New York, New Jersey, Texas, and South Carolina, along with a “Combined Excise Tax Return” that reported state sales and use tax for the state of Washington, and a return reporting state, county and transit sales tax for Ohio for the same period. Carfax made sales of VHRs in these states, and paid tax on those sales. *See* Pet. Ex. 13; App. 30. As Mr. Corr explained, Carfax sold no other taxable products in those states during the Tax Period. Carfax determined the states where the reports were taxable by engaging the accounting firm PwC to analyze the applicable statutes, and through ongoing review and analysis of the statutes in the various states. Tr. 108-109. Based on Mr. Corr’s testimony and the sales and use taxes reported on the returns included in Petitioner’s Exhibit 13, it is reasonable to conclude that Carfax’s sales of VHRs were subject to sales or use tax in New York, New Jersey, Texas, Washington, South Carolina, and Ohio during the periods at issue in this case.

On the other hand, it is unreasonable to conclude that Carfax, its parent company, its in-house team of tax professionals, and the professionals at PwC who were consulted

on this issue decided that tax should be paid tax on Carfax's VHR sales in these six states despite any legal obligation to do so. *See* Tr. 108-109. Further, Petitioner's Exhibit 13 reveals that the amount of tax paid by Carfax each month on these transactions is significant. *See* Pet. Ex. 13; App. 30. Regardless, the Director has not cited any statutes or evidence that indicate these sales were not subject to sales or use tax.

Even assuming *arguendo* that the evidence had not established this as a fact, whether Carfax's VHR sales were actually subject to tax in another state is a legal issue that is established by Texas Tax Code §§ 151.0101(a)(12) and 151.0035. The parties agreed that the Commission can take official notice of the statutes of other states. *See* Tr. at 8. This is consistent with § 536.070(6), RSMo, which provides that "[a]gencies shall take official notice of all matters of which the courts take judicial notice" and § 490.080, RSMo, which states that "[e]very court of this state shall take judicial notice of the common law and statutes of every state, territory and other jurisdiction of the United States." Carfax submitted a motion at the outset of the Evidentiary Hearing in this case asking the Commission to take official notice of §§ 151.0101(a) and 151.0035 of the Texas Tax Code.

Upon analyzing these provisions, it is evident that Carfax's VHR sales are subject to sales and use tax in Texas. Section 151.0101(a) of the Texas Tax Code provides a list of services taxable under Texas's sales and use tax law. Among those taxable services is "data processing services." *See* Tex. Tax Code § 151.0101(a)(12). In turn, "data processing services" is defined by Texas law to include "information compilation" as well as, among other things, "other computerized data and information storage or manipulation." *See* Tex. Tax Code § 151.0035. Since Carfax's sale of VHRs included "information compilation,"

as well as “computerized data and information storage or manipulation” they fall within the Texas definition of taxable “data processing services.” Carfax’s sales of VHRs are subject to Texas sales and use tax under these statutes. Other state statutes also plainly require Carfax to collect sales or use tax on its sales of VHRs. *See, e.g.*, New York Tax Law § 1105(c)(1) (imposing New York sales tax on the service of “furnishing of information by printed, mimeographed or multigraphed matter or by duplicating written or printed matter in any other manner, including the services of collecting, compiling or analyzing information of any kind or nature and furnishing reports thereof to other persons . . .”).

Consistent with this legal conclusion, the Texas sales and use tax return included in Petitioner’s Exhibit 13 demonstrates that Carfax had gross receipts from the retail sales of VHRs in Texas during the audit period at issue in this case, and paid Texas state and local use tax on these sales. *See* Tr. 112-113. Therefore a VHR is a service subject to sales or use tax in a state other than Missouri, which means a VHR comes within § 144.010.1(9)’s definition is a “product which is intended to be sold ultimately for final use or consumption” and for the purposes of § 144.030.2(5).

III. The Director’s interpretation of § 144.010.1(9) is inconsistent with the plain language of the statute, the reasonable expectations of the General Assembly, and the Director’s own regulations. (Response to Appellant’s Point II(B)).

In addition to misstating the Commission’s ruling concerning whether Carfax was liable for taxes on its sales of VHRs in other states, the Director has proposed a tortured and unreasonable interpretation of the term “product intended to be sold for final use or

consumption.” This term is defined by § 144.010.1(9) as follows:

“Product intended to be sold for final use or consumption means tangible personal property, or **any service that is subject to state or local sales or use taxes**, or any tax that is substantially equivalent thereto, **in this state or any other state.**”

(emphasis added). Consistent with the commonly understood meaning of these words, as well as the Director’s own regulations, the Commission concluded that because Carfax established that its sales of VHRs were services subject to sales and use tax in states other than Missouri, the VHRs were “intended to be sold ultimately for final use or consumption.” L.F. 59; App. 125. The Director’s arguments to the contrary misconstrue this language, and as noted above, fail to recognize that the Commission expressly found that “Carfax established that it was liable for sales and use tax [on sales of VHRs] during the audit period in states other than Missouri.” L.F. 59-60; App. 125.

Regulations promulgated by the Director support Carfax. Specifically, in 12 C.S.R. § 10-111.010(2)(I), the Director has interpreted § 144.010.1(9) by providing the following expanded definition:

(I) Product which is intended to be sold ultimately for final use or consumption—Tangible personal property, or any service that is subject to state or local sales or use taxes, or any tax that is substantially equivalent thereto, in this state or any other state, which is intended at the time of manufacturing, mining or fabrication to be sold at retail. Property or services cannot be considered to be “subject to” the tax of a state unless the property or services are actually to be sold at retail in that state or delivered to a retail customer in that state.

12 C.S.R. § 10-111.010(2)(I), App. 129. The regulation further provides the following examples:

(J) A taxpayer creates and sells a nontaxable information service product. To develop its product, taxpayer purchases computer hardware and software. Because taxpayer produces a nontaxable service product, it is not manufacturing a product intended to be sold ultimately for final use or consumption and, therefore its purchases of computer equipment are not exempt from tax.

* * *

(P) A taxpayer sells and installs computer hardware and software and provides information technology services to its customers. The hardware and software are tangible personal property subject to sales tax. **The technology services are not subject to tax in Missouri but are subject to tax and the taxpayer remits sales tax to Texas.** The taxpayer's purchase of machinery and equipment to develop its products and services is intended to manufacture a taxable product or a taxable service intended to be sold ultimately for final use or consumption. The purchase of machinery and equipment is exempt from tax.

12 C.S.R. § 10-111.010(4)(J) and (P); App. 129. These two examples highlight the distinction between a “non-taxable service” and a service that is taxable in Texas but not Missouri. The Director’s regulation recognizes that the service subject to tax in Texas but not Missouri qualifies as “a product which is intended to the sold ultimately for final use or consumption.” This is exactly the situation at issue in Carfax’s case.

In his brief, however, the Director takes an entirely different approach. The Director inaccurately imports a requirement that the property or service must be subject to Missouri state or local sales or use tax. *See App. Br. at 41.* The Director’s reading of § 144.010.1(9) can be re-stated as follows:

Product intended to be sold for final use or consumption means tangible personal property, or any service that is subject to [Missouri] state or local sales or use taxes or [that would be

subject to Missouri state and local sales or use tax if it were sold in this state].

App. Br. at 38-41. This completely re-writes § 144.010.1(9) by effectively inserting the words in brackets above and substituting them for the actual language of the statute. The Director’s interpretation of the statute ignores the fact that the terms “sales and use taxes” have commonly understood meanings. App. Br. at 39. The dictionary defines “sales tax” as “a tax levied on the sale of goods and services that is usually calculated as a percentage of the purchase price and collected by the seller.” *See* Merriam-Webster.com. The term “use tax” is defined by the dictionary as “a tax imposed on the use of personal property and especially property purchased in another state.” *Id.* As shown by the tax returns included in Petitioner’s Exhibit 13, other states have “sales and use taxes” that come within these definitions. *See* Pet. Ex. 13; App. 30. There are, however, several states that impose similar taxes that are not technically “sales and use taxes.” For example, in Illinois, the “Retailers’ Occupation Tax” or “R.O.T” is “imposed upon persons engaged in the business of selling at retail tangible personal property” and is based on a percentage of the seller’s gross receipts from such sales. *See* 35 ILCS §§ 120/2 and 120/2-10. Arizona’s “sales tax” is the “Transaction Privilege Tax,” which is imposed for the privilege of doing business in the state. Ariz. Rev. Stat. § 42-5008. Retailers are liable for this tax, which they may pass on to their customers. Ariz. Rev. Stat. § 42-5061. The tax is based on a percentage of a retailer’s gross receipts. Ariz. Rev. Stat. § 42-5010. These are examples of taxes that are technically not “sales or use taxes,” in that they are not imposed directly on “sales” but are

“substantially equivalent thereto.” This is the type of tax imposed by states other than Missouri to which the statute refers.

Contrary to the Director’s assertions, the phrase: “tangible personal property, or any service that is subject to state or local sales or use taxes, or any tax that is substantially equivalent thereto, in this state or any other state” means simply that the product at issue must be:

- subject to a state or local sales or use tax *or*
- subject to a tax that is substantially equivalent to a sales or use tax,
- in either Missouri or some other state.

This is the meaning of the plain language, which is consistent with the Director’s regulations and should be followed by this Court.

The Director points to the fact that this definition was enacted by the legislature in 1998 in S.B. 936, following this Court’s December 1997 decision in *Int’l Bus. Machines, supra*. App. Br. at 40. But if the Director’s interpretation of the statute is correct, then this legislation made no change to the existing law, since the holding in *Int’l Bus. Machines* established that a “product which is intended to be *sold* ultimately for final use or consumption” includes only those services that are subject to Missouri sales tax. As the Court explained:

“Sale” thus includes both selling tangible personal property and rendering taxable services. By the 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.

958 S.W.2d at 557-558.

The Court’s decision *Int’l Bus. Machines* does not address taxes imposed by other states. By including language that refers not only to “sales and use taxes,” but also taxes that are “substantially equivalent” to sales and use tax, as well as taxes imposed by other states—it is clear that the legislature’s purpose in enacting § 144.010.1(9) was *not* merely to codify the holding of *Int’l Bus. Machines*, but instead to include within the definition products subject to sales or use tax in other states, in addition to those that are subject to tax in Missouri.

The Director also asserts that because one purpose of the manufacturing exemptions is to encourage the production of items subject to sales tax in Missouri, § 144.010.1(9) cannot be interpreted to include VHRs, since they are not subject to Missouri tax. App. Br. at 37. But it is also well-established that the manufacturing exemptions serve the purpose of encouraging the location and expansion of industry in Missouri. *See Concord Publishing House, Inc. v. Director of Revenue*, 916 S.W.2d 186, 190 (Mo. banc 1996) and cases cited therein. This purpose is served by upholding the exemptions in Carfax’s case.

Most importantly, since the language of the statute is clear and unambiguous this Court’s analysis should end there. As this Court explained in *Jones v. Director of Revenue*, 832 S.W.2d 516, 517 (Mo. banc 1992): “[t]he primary rule of statutory construction requires this Court to ascertain the intent of the legislature by considering the plain and ordinary meaning of the words used in the statute. *Union Elec. Co. v. Director of Revenue*, 799 S.W.2d 78, 79 (Mo. banc 1990). Where the language of the statute is clear and unambiguous, there is no room for construction. *Community Federal Savings and Loan Ass’n v. Director of Revenue*, 752 S.W.2d 794, 798 (Mo. banc 1988). If terms within a tax

statute are defined by the legislature, this Court must give effect to the legislature's definition. *St. Louis Country Club v. Administrative Hearing Commission*, 657 S.W.2d 614, 617 (Mo. banc 1983).” The legislature has defined “product which is intended to be sold ultimately for final use of consumption” for the purposes of § 144.030.2(5). The language of this statutory definition is clear and unambiguous, and it encompasses the VHRs sold by Carfax, because the VHRs are subject to sales and use tax in another state.

The Director’s approach should be rejected because it is inconsistent with the statute’s plain language. Moreover, because the Director’s approach is inconsistent with the regulations noted above, any decision of this Court adopting the Director’s interpretation of this statute would be an “unexpected decision” within the meaning of § 143.903, which provides in pertinent part:

1. Any provision of law to the contrary notwithstanding, an unexpected decision by or order of a court of competent jurisdiction or the administrative hearing commission shall only apply after the most recently ended tax period of the particular class of persons subject to such tax imposed by chapters 143 and 144 and any credit, refund or additional assessment shall be only for periods after the most recently ended tax period of such persons.
2. The provisions of this section shall apply only to final decisions by or orders of a court of competent jurisdiction or the administrative hearing commission which are rendered after October 1, 1990, and which are determined by the court or the administrative hearing commission rendering the decision, or subsequently by a lower court or the administrative hearing commission, to be unexpected. For the purposes of this section the term “unexpected” shall mean that a reasonable person would not have expected the decision or order based on prior law, previous policy or regulation of the department of revenue.

This section recognizes that taxpayers have a right to rely on regulations published by the Director. Because the Director has changed his interpretation of the law in a way that is inconsistent with existing regulations, a decision of this Court adopting this interpretation may only apply prospectively—not to the past tax periods at issue in this case.

Finally, as noted above, even if this Court were to conclude that a VHR is not a “product which is intended to be sold ultimately for final use or consumption” within the meaning of § 144.010.1(9), it should nonetheless uphold the Commission’s ruling that all of the purchases by Carfax that are at issue in this case are exempt under § 144.054.2. Section 144.054.2 does not require that that VHRs be subject to sales or use tax in order to be considered a “product.”

CONCLUSION

The Commission’s decision in this case is authorized by law, supported by competent and substantial evidence, and consistent with the reasonable expectations of the General Assembly. The decision is consistent with this Court’s decisions in both *IBM* and *DST*, and does not expand the scope of the manufacturing exemptions. Carfax respectfully requests that this Court affirm the Commission’s decision that Carfax is entitled to an exemption from sales and use tax under §144.054.2 for all of the machinery and equipment at issue in this case and under § 144.030.2(5) for all of its purchases at issue except the conferencing equipment.

Respectfully submitted,

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Dated: March 18, 2022

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CERTIFICATE OF SERVICE AND COMPLIANCE

I hereby certify that the foregoing was electronically mailed to Michael Talent, Assistant Attorney General, Missouri Attorney General's Office, Supreme Court Building at Michael.Talent@ago.mo.gov on March 18, 2022.

I also hereby certify that the foregoing brief complies with Rule 55.03 and with the limitations in Rule 84.06(b) in that it contains 12,301 words.

/s/ Carole L. Iles