IN THE SUPREME COURT OF MISSOURI

No. SC91471

KRISPY KREME DOUGHNUT CORPORATION,
Appellant,

v.

DIRECTOR OF REVENUE,
Respondent.

ON PETITION FOR REVIEW
FROM THE MISSOURI ADMINISTRATIVE HEARING COMMISSION,
THE HONORABLE KAREN A. WINN, COMMISSIONER
No. 06-1044 RS

APPELLANT'S REPLY BRIEF

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INTRODUCTION

This appeal is about the proper amount of tax that bakeries like Appellant Krispy Kreme Doughnut Corporation ("Krispy Kreme") must charge their customers for food items and subsequently remit to Respondent, the Missouri Director of Revenue (the "Director"). Section 144.014 of the Revised Statutes of Missouri expressly provides that a special food sales tax rate applies to retail sales of food of the type that may be purchased with federal food stamps. Section 144.014 only requires that, in order to charge the food tax rate, food establishments must derive at least 20 percent of their total gross receipts from the sale of products other than "food prepared … for immediate consumption." To extract the maximum amount of revenue from Krispy Kreme's customers, the Director construed the term "food prepared … for immediate consumption" to denote solely "ready-to-eat" food. The Administrative Hearing Commission (the "Commission") endorsed this erroneous construction.

In its opening brief, Krispy Kreme demonstrated that this cramped reading of section 144.014 cannot be reconciled with the plain language of the statute, the federal law to which section 144.014 looks for guidance, the settled industry understanding, the decisions of other states' highest courts, or the Director's own regulations. The Director barely attempts to marshal a response to these arguments or to defend the Commission's construction.

Instead, the Director embarks on an extensive attempt at misdirection, mischaracterizing Krispy Kreme's position, inverting the statutory text and purpose,

ignoring the record, and reversing the positions she advocated below. The only constant fixture in the Director's argument is that she should be entitled to collect the highest possible sales tax rate on food stamp-eligible items. This position, however, is squarely foreclosed by the plain text of section 144.014, as well as by the relevant federal law and judicial authority. Nor can this approach be reconciled with the statutory purpose, which is to facilitate purchases of qualified food items. Critically, the Director's litigation-driven position cannot be squared with her own published regulations — a conflict that the Director altogether fails to address, much less to resolve. This Court should correct the Commission's erroneous statutory construction, and reaffirm that retail bakeries selling food products otherwise qualified for the food tax rate under Missouri law are required to charge their customers the lower food tax rate.

ARGUMENT

I. THE PLAIN LANGUAGE OF SECTION 144.014 SUPPORTS KRISPY KREME'S STATUTORY CONSTRUCTION, AND IS ANTITHETICAL TO THE DIRECTOR'S INTERPRETATION.

The Director concedes that section 144.014 is unambiguous, and that its plain language should therefore govern. Resp't Br. 17; *see also* Resp't Br. 20. The Director, however, profoundly misreads the statutory text. By its plain terms, section 144.014 requires an establishment selling food stamp-qualified food to charge its customers the lower sales tax rate, provided only that no more than 80 percent of the establishment's total gross receipts are derived from the sale of food that is "prepared by such

establishment for immediate consumption." § 144.014.2.[1] The language of section 144.014 forecloses the Commission's erroneous construction of the term "food prepared … for immediate consumption" to mean food "'needing no further preparation.'" L.F. 378. This interpretation reads out of the statute the temporal requirement that consumption of food follow its preparation without delay and nullifies section 144.014's express reference to "restaurant[s]" and "fast food restaurant[s]" as types of establishments that could charge the food tax rate. *See* Appellant Br. 22-25.

The Director's attempt to defend the Commission's construction is half-hearted at best. *See* Resp't Br. 17, 29. Accusing Krispy Kreme of ignoring the "critical term 'prepared,'" the Director argues that a proper construction of section 144.014 must "focus[] on the state of the preparation of the food and not on the timing of actual consumption." Resp't Br. 20-21; *see also* Resp't Br. 17.

As the Director acknowledges, the dictionary definition of the term "prepare" is "to make ready beforehand for some purpose" or, as particularly relevant, "to make ready for eating." *Webster's Third New International Dictionary* 1790 (1993), *quoted in* Resp't Br. 20; *see also* Appellant Br. at 35. Under this definition, the term "prepared food"

[1] The complete text of section 144.014 is included in the Appendix to Appellant's Brief at A16. Unless otherwise noted, all Missouri statutory citations are to the Revised Statutes of Missouri, R.S. Mo. 2010. "L.F." refers to the Legal File.

denotes "food [that is] ma[d]e ready for eating."[2] This definition, however, is indistinguishable from the construction that the Director (and the Commission) gave to the entire statutory phrase "food prepared … for immediate consumption," construing it as "food [that is] read[y] to be consumed without further preparation." Resp't Br. 29; *see also* L.F. 378 (adopting the Director's definition). Thus, under the interpretation advanced by the Director, the remaining terms of section 144.014.2 — "immediate" and "consumption" — become entirely superfluous. *See* Appellant Br. 35. As this Court instructed, however, proper statutory interpretation must presume that the legislature did not intend to include superfluous language. *Norwin G. Heimos Greenhouse, Inc. v. Dir. of Revenue*, 724 S.W.2d 505, 508 (Mo. banc 1987).[3]

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[2] As Krispy Kreme noted, this is precisely how the Missouri legislature defined the term "prepared food" in other contexts, *see, e.g.*, section 192.081.1(6) — a fact of which the legislature is presumed to have been aware when it enacted section 144.014, *Nicolai v. City of St. Louis*, 762 S.W.2d 423, 426 (Mo. banc 1988). *See* Appellant Br. 35 n.18.

[3] The Director's attempt to shore up the Commission's construction by reference to section 144.014's provision that food may be considered as "prepared by [an] establishment for immediate consumption" "regardless of whether such prepared food is consumed on the premises of that establishment," misses its mark. Contrary to the Director, that provision does not indicate that section 144.014 "rejects any notion that the time between preparation and actual consumption matters." Resp't Br. 24. Rather, it merely ensures that such food establishments that have on-premises facilities but often

Contrary to the Director's claim, Krispy Kreme's reading of section 144.014 does not overlook the fact that the term "immediate consumption" is "attach[ed]" to the term "prepared." Resp't Br. 21. Rather, it is the Director's interpretation that ignores altogether the statutory interplay between the terms "prepared" and "immediate consumption," and reads the latter term out of the statute. This construction is flatly contrary to this Court's admonition that "words used in proximity to one another must be considered together." *Albanna v. State Bd. of Registration for Healing Arts*, 293 S.W.3d 423, 431 (Mo. banc 2009).

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sell their products to be consumed outside (such as ice cream shops) or such food establishments that offer no on-premises seating facilities (such as street vendors and mobile food carts) are encompassed by the 80/20 rule. *See* Appellant Br. 45-46. That does not eliminate the need for a temporal connection between the preparation of food and its consumption. An ice cream cone will be eaten without delay after its preparation irrespective of whether the customer does so on the store premises or while walking away. The relevant federal regulations reinforce this view. They expressly define food "served for immediate consumption" as food designed to be eaten without delay, irrespective of whether the customer "consume[s the food] immediately where purchased or while … walking away." 21 C.F.R. § 101.9(j)(2)(ii); *see also* Appellant Br. 29, 45-46; Br. of *Amici Curiae* Retail Bakers of Am. and Am. Bakers Ass'n in Supp. of Appellant 8-9.

II. THE DIRECTOR'S INTERPRETATION CANNOT BE RECONCILED WITH THE CONSTRUCTION OF ANALOGOUS STATUTORY TERMS BY OTHER STATE HIGHEST COURTS, U.S. CONGRESS, AND FEDERAL REGULATORY AUTHORITIES.

As Krispy Kreme demonstrated, its construction of section 144.014 comports fully with the construction of analogous statutory terms by other state highest courts, federal law, and food industry understanding. *See* Appellant Br. 25-29, 33-35, 42-43. The Director barely offers any response to Krispy Kreme's arguments, effectively conceding their validity.

The Director asserts that the opinion of the Supreme Court of Illinois in *Canteen Corporation v. Department of Revenue*, 525 N.E.2d 73 (Ill. 1988), supports her contention that the plain language of section 144.014 focuses solely "on the state of the *preparation* of the food items, and not on the timing of actual consumption." Resp't Br. 17 (citing *Canteen Corp.*, 525 N.E.2d at 77) (emphasis in the original). The *Canteen* court, however, held precisely the opposite. The court concluded that a variety of ready-to-eat food items sold through vending machines nevertheless did not constitute "food … prepared for immediate consumption" under the Illinois law. Although these items were "ready to eat before they are even placed in the vending machines, much less sold," the *Canteen* court nevertheless held that such items are not "prepared for immediate consumption" because "[f]or those items, there is *a substantial delay* between the final stage of preparation and the time of consumption." 525 N.E.2d at 78 (emphasis added).

Thus, the touchstone of interpreting section 144.014's term "food prepared … for immediate consumption" must be the temporal relationship between the food's preparation and its consumption. A contrary approach disregards this Court's instruction that "[e]ach word, clause, sentence and section of a statute should be given meaning." *State ex rel. Womack v. Rolf*, 173 S.W.3d 634, 638 (Mo. banc 2005) (internal quotation marks and citation omitted).

The Director fails to mention that, in examining the meaning of the term "prepared" the *Canteen* court concluded that

> [t]he plain and common meaning of the term "prepare" is *to make ready*. In the context of food for human consumption, food preparation would include the steps or acts necessary to make the food *ready to eat*.

Canteen Corp., 525 N.E.2d at 77 (emphasis added); *see also* Appellant Br. 34-35. Thus, the Illinois Supreme Court expressly defined "food which has been prepared" as "food [that is] ready to eat," *Canteen Corp.*, 525 N.E.2d at 77 (internal quotation marks omitted) (emphasis removed) — the meaning that the Director now seeks to assign to the broader term "food prepared … for immediate consumption" in section 144.014. *See* Resp't Br. 17, 29.

Importantly, the Supreme Court of Illinois proceeded to examine the separate statutory term "'immediate,'" which it deemed to be "of special significance." *Canteen Corp.*, 525 N.E.2d at 77. In doing so, the *Canteen* court distinguished between two

subclasses of food that has been "prepared for consumption": (1) "food 'prepared for immediate consumption' — *that is, food made ready to be eaten without substantial delay* —" and (2) "food which has reached its final stage of preparation but *which is to be eaten only after a delay or at a later time*." *Id.* (emphasis added). Thus, the *Canteen* court recognized that the term "immediate consumption," when used in a statutory phrase "'food which has been prepared for immediate consumption,'" necessarily includes a temporal element, and refers to food "made ready to be eaten without substantial delay." *Id.* at 76, 77. As the Illinois Supreme Court explained, "[a]ll food sold at retail has been either prepared for consumption or not," and so "food prepared for *immediate* consumption must therefore be *a subclass* of food prepared for consumption" (*i.e.*, of food that is "ready to eat"). *Id.* at 77 (second emphasis added). The *Canteen* court's conclusion that the term "'food … prepared for immediate consumption'" means "food made ready to be eaten without substantial delay," *id.* at 76, 77, is irreconcilable with the Director's insistence that the identical term in section 144.014 denotes all food that is "read[y] to be consumed without further preparation," Resp't Br. 29; *see also* Resp't Br. 17.

The *Canteen* court's analysis is fully in accord with the approach adopted by relevant federal law and regulations. As Krispy Kreme demonstrated, federal law distinguishes between food that is "ready for human consumption" and food that is offered "for immediate human consumption." 21 U.S.C. § 343(q)(5)(A)(ii); *see also* 21 C.F.R. § 101.9(j)(3)(ii), (iii) (same); *Food Labeling; Nutrition Labeling of Standard*

Menu Items in Restaurants and Similar Retail Food Establishments, 76 Fed. Reg. 19,192, 19,196 (proposed Apr. 6, 2011) (explaining the statutory difference between the two categories); Appellant Br. 26-28 & n.12; Br. of *Amici Curiae* Retail Bakers of Am. and Am. Bakers Ass'n in Supp. of Appellant ("*Amici* Br.") 11-13. As *Amici Curiae* Retail Bakers of America ("RBA") and America Bakers Association ("ABA") (collectively, "*Amici* Associations") observed, federal law "rejects a definition of 'for immediate consumption' that equates the term with 'ready-to-eat.'" *Amici* Br. 11.

In a cursory footnote, the Director blithely dismisses federal regulations as irrelevant because they "deal merely with food labeling." Resp't Br. 28-29 n.4. But the Director offers no response whatsoever to Krispy Kreme's and the *Amici* Associations' argument that the approach adopted by the federal regulators reflects the accepted meaning of the term "immediate consumption," as used in the food industry (and the baking industry in particular). *See* Appellant Br. 25-26; *Amici* Br. 8-9, 13. In the absence of a specific legislative or judicial definition of the relevant statutory term, this Court considers industry practice as informative as to the term's meaning. *Walsworth Pub. Co., Inc. v. Dir. of Revenue*, 935 S.W.2d 39, 40 (Mo. banc 1996). The Director offers no reason why this Court should depart from this settled practice in this case.

The Director ignores altogether the fact that section 144.014 expressly looks towards a specific federal legal regime — the federal food stamp program. *See* section 144.014.2 (referring to 7 U.S.C. § 2012 — the federal statute governing the federal food stamp program — when defining qualified food under section 144.014); *see also*

Appellant Br. 6, 26; *Amici* Br. 2. Given this express reliance on a federal scheme, it is simply not reasonable that the Missouri legislature would have been unaware of the way in which the federal law defines the term "immediate consumption" or would have intended to enact into Missouri law a definition that is demonstrably at odds with the federal one.

III. KRISPY KREME'S REFUND CLAIM FULLY COMPORTS WITH SECTION 144.014'S DEFINITION OF "FOOD PREPARED … FOR IMMEDIATE CONSUMPTION."

Recognizing the infirmity of her Arguments, the Director embarks on an attempt at misdirection, arguing that Krispy Kreme's basis for its refund claim is either internally inconsistent or outcome oriented. None of the arguments proffered by the Director, however, holds any merit.

The Director contends — without any reference to the record — that Krispy Kreme "conceded" that "the great majority of its retail sales are of doughnuts that … are actually immediately consumed." Resp't Br. 18. Krispy Kreme made no such concession, nor is there any evidence to support the Director's assertion. In fact, Krispy Kreme's unchallenged evidence demonstrates that between 57.89 (100%-42.11%) and 91.51 (100%-8.49%) percent of doughnuts purchased at its Missouri stores were not consumed on the premises or while traveling away from the store, but were taken to an entirely separate location. L.F. 029-032; *see also* L.F. 026-027 (¶ 8).

Although Krispy Kreme excluded from its refund claim sales of doughnuts consumed by customers on the premises of its stores, *see* L.F. 025 (¶ 5); L.F. 039 (¶ 6); L.F. 366-67 (¶ 9); Appellant Br. 10, that is not a concession that such doughnuts, assuming they were prepared well in advance of consumption, are "immediately consumed." Krispy Kreme excluded its "dine-in" sales of food otherwise qualifying under section 144.014 because the Director's regulation interpreting section 144.014 expressly disqualifies sales of qualified food from receiving the lower sales tax rate of section 144.014 if such food "is consumed on the premises." 12 CSR 10-110.990(3)(H), *included at* L.F. 041 and A17.[4] Although the basis for the Director's interpretation is unclear, Krispy Kreme nevertheless decided to follow the Director's published regulations — something that the Director herself is apparently unwilling to do, *see* Appellant Br. 38-39; *infra* at 25-26.

Similarly misleading is the Director's contention that "Krispy Kreme … does not argue that most doughnuts purchased at its drive-throughs are not prepared for immediate consumption." Resp't Br. 18. The Director does not explain how this fact — assuming, *arguendo*, it were true — is relevant to Krispy Kreme's argument that at least 20 percent

[4] This appeal, therefore, does not involve the issue that the Director urges this Court to address in *Wehrenberg, Inc. v. Director of Revenue*, No. SC91283, scheduled for argument on the same day as the instant appeal — namely, whether otherwise qualified food that is packaged for on-premises consumption ceases to be qualified food for the purposes of section 144.014.

of its doughnuts were not prepared for immediate consumption because they were prepared an hour or more beforehand, regardless of whether they were sold at the drive-through. Nor is there any evidence in the record to support the Director's conclusion that "most" doughnuts bought at drive-throughs were eaten immediately, in the car. In any event, even allowing for such an inference, a survey that Krispy Kreme conducted of *all* the purchases made at its Missouri stores demonstrates that well over 20 percent of Krispy Kreme's retail sales derived from products that its customers consumed in other locations, and not on the premises or while walking away from the store. *See* L.F. 026-27 (¶ 8); L.F. 029-32; L.F. 366 (¶ 6); Appellant Br. 5. Indeed, this survey disclosed that an overwhelming majority of these retail purchases — between 57.89 and 91.51 percent — were not consumed on the premises or while traveling away from the store. L.F. 029-032; *see also* L.F. 026-027 (¶ 8); *supra* at 10.

The Director next chastises Krispy Kreme for not referring to its trademark — "HOT DOUGHNUTS NOW." Resp't Br. 18. Aside from a conclusory assertion that such advertisement is "fundamentally inconsistent" with Krispy Kreme's argument, Resp't Br. 10, the Director does not explain how this sign is relevant to the legal analysis. As the Director concedes, "[t]he words 'HOT' and 'NOW' are only turned on for advertising when the original glaze doughnuts are being made and available for customers." Resp't Br. 4-5 (citing L.F. 304). Unchallenged evidence presented by Krispy Kreme demonstrated that glazed doughnuts are made only two times during the day: early in the morning and after 5:30 in the afternoon. L.F. 035 (¶ 6); *see also*

Appellant Br. 3. The words "HOT" and "NOW" are turned on during these two times precisely because the majority of the time, the doughnuts offered by Krispy Kreme are not hot.

As Krispy Kreme established, sales of its doughnuts prepared at least one hour prior to sale, and so necessarily prior to consumption, combined with sales of drinks prepared elsewhere, constituted between 31.25 and 56.3 percent of total retail sales. L.F. 035-36 (¶ 8); *see also* Appellant Br. 4, 32. "One or more hours after preparation, even the glazed doughnuts are no longer warm." L.F. 146 (¶ 3). As the Director's own regulations acknowledge, "[b]akery items, even if still warm from baking, are qualified foods" under section 144.014. 12 CSR 10-110.990(2)(A), *included at* L.F. 041 and A17; *see also* Mo. Dep't of Revenue, *Missouri Sales Tax Reduction on Food* (2009), http://dor.mo.gov/tax/business/sales/foodtax.htm, *included at* L.F. 42 and A18 (tax policy notice indicating that even when "donuts may still be warm from baking, the donut sales are taxed at the reduced rate"). Thus, the fact that, on two limited occasions during the day, Krispy Kreme stores turn on the words "HOT" and "NOW" in their window signs supports, rather than undermines, Krispy Kreme's argument.

Finally, the Director persists in repeating her erroneous contention below that Krispy Kreme's filings with the Securities and Exchange Commission ("SEC") "characterize" its Missouri store locations as "'restaurants.'" Resp't Br. 4; *see also* L.F. 305 & n.1. As Krispy Kreme explained below, in an unchallenged affidavit, these SEC filings are those of its *parent* corporation, Krispy Kreme Doughnuts, Inc. L.F. 343

(¶ 2). Moreover, these filings list Krispy Kreme's parent corporation under Standard Industrial Classification ("SIC") code 5400, which is designed for "retail stores primarily engaged in selling food for home preparation and consumption." *Id.* Included in this overall code are "grocery stores (code 5411) and retail bakeries (code 5461)." L.F. 344 (¶ 2); *see also* L.F. 333-34. As Krispy Kreme demonstrated — and as the Director did not challenge, *see* L.F. 333 — Krispy Kreme "is engaged in the bakery business" under the SIC code 2051 ("manufacturing bread, cake and related products") and the North American Industry Classification System ("NAICS") code 311812 ("producing bakery products made in commercial bakeries"). L.F. 023-24; *see also* L.F. 334; L.F. 343-44 (¶ 2).

There is, therefore, no basis in the record for the Director's repeated attempts to mischaracterize Krispy Kreme's Missouri stores as "fast food doughnut restaurants." *See, e.g.*, Resp't Br. 19, 30, 31. This characterization is entirely at odds with the fact that *over 30 percent* of sales at Krispy Kreme's Missouri stores were wholesale sales of doughnuts to retailers, who then resold those doughnuts. *See* L.F. 024 (¶ 3); L.F. 365 (¶ 3); Appellant Br. 3-4. It is hard to conceive of a "fast food restaurant" where approximately one-third of sales are for wholesale, not retail. Nor can the Director's view of Krispy Kreme be squared with the fact that the ABA — an association of the wholesale baking industry and its members' retail outlets, *Amici* Br. 1 — considered it important enough to lend its support to Krispy Kreme's argument as an *amicus*.

IV. THE THREE INDEPENDENT BASES OFFERED BY KRISPY KREME IN SUPPORT OF ITS REFUND CLAIM ARE REASONABLE AND SEEK TO EFFECTUATE SECTION 144.014'S REQUIREMENTS.

The Director's assertion that the three independent bases (and supporting evidence) that Krispy Kreme offered in support of its refund claim are "purely outcome oriented," Resp't Br. 18, is meritless. Krispy Kreme offered three independent bases because interpretation of section 144.014 is a matter of first impression for this Court. There is not a shred of support in the record for the Director's accusation that, in analyzing its doughnut sales, Krispy Kreme selected its criteria in order to fit some pre-conceived outcome.

On the contrary, the record conclusively refutes any such assertion. Thus, the Director contends that the one-hour period selected by Krispy Kreme in order to determine the quantity of its doughnuts prepared in advance of consumption "is purely arbitrary — other than it conveniently allows Krispy Kreme to claim a reduced tax rate." Resp't Br. 22. If, indeed, Krispy Kreme had selected the one-hour period purely in order to meet section 144.014's 80/20 rule, one would expect a result that is fairly close to that rule's 20-percent cut-off mark. The record discloses, however, that under the one-hour yardstick, *between 31.25 and 56.3 percent* of Krispy Kreme's total retail sales consisted of doughnuts prepared at least one hour prior to consumption, combined with sales of foods not prepared by Krispy Kreme. L.F. 035-36 (¶ 8); *see also* Appellant Br. 4.

Moreover, this calculation intentionally *underestimated* the amount of doughnuts that were prepared at least an hour in advance of consumption. Krispy Kreme found it difficult to estimate the number of glazed doughnuts sold in the morning that were prepared more than one our prior to sale. L.F. 035 (¶ 7). Krispy Kreme therefore applied a deliberately "incorrect assumption that all of [Krispy Kreme]'s sales of glazed donuts in the morning were prepared within on[e] hour of the time they were sold," thereby excluding *all* such doughnut sales from sales it used to meet the one-hour threshold for the purposes of satisfying the 80/20 rule. L.F. 035-36 (¶ 8). Given that "[h]alf of the glazed donuts sold after noon were prepared more than one hour prior to their sale," L.F. 035 (¶ 7), the overall percentage of Krispy Kreme's doughnuts prepared more than an hour prior to consumption is likely even higher.[5]

Grasping at straws, the Director next contends that Krispy Kreme's construction of section 144.014 would "produce[] absurd results" because it would "subject the entire restaurant to different tax rates merely on the basis of which [doughnut] was picked up first by the employee." Resp't Br. 22. This argument profoundly misunderstands how section 144.014's 80/20 rule operates. As Krispy Kreme explained in its opening brief

[5] In addition, many of the doughnuts were prepared much earlier than an hour prior to their sale (and, therefore, prior to consumption). The record discloses that *all* cake and processed doughnuts were prepared during the shift prior to the one when they were sold. L.F. 035 (¶ 6). This fact further refutes the Director's suggestion that Krispy Kreme selected the one-hour period in order to scrape past the 20-percent threshold.

— an explanation that the Director ignores entirely — the 80/20 rule focuses on whether a particular *establishment* qualifies to make any sales at the food tax rate. *See* Appellant Br. at 30. To do so, the rule examines whether "the *total* gross receipts of [an] establishment" are such that its sales of "food prepared by such establishment for immediate consumption" constitute more than 80 percent of the total gross receipts. Section 144.014.2 (emphasis added). If the establishment satisfies this rule, then it may sell *all* food that qualifies under section 144.014 (*i.e.*, food stamp-eligible food) at the lower sales tax rate. *See* Appellant Br. at 30. Thus, there is no danger whatsoever of an establishment becoming "subject … to different tax rates" for the same food product under Krispy Kreme's interpretation. If Krispy Kreme's stores satisfy the 80/20 rule — that is, if at least 20 percent of their total sales are not sales of "food prepared by [an] establishment for immediate consumption" — then Krispy Kreme may sell all of its eligible foods at the food tax rate.[6]

[6] Krispy Kreme also explained why *Canteen Corporation*, which both the Commission and the Director invoke to shore up their arbitrariness concern, *see* L.F. 375; Resp't Br. 22, is inapposite in this respect. *See* Appellant Br. 31 n.15. The Illinois state statute at issue in *Canteen* was food-specific, not establishment-specific. That statute provided that the food sales tax shall not apply to *any* specific "'food … prepared for immediate consumption.'" 525 N.E.2d at 76 (quoting Ill. Rev. Stat. 1981, ch. 120, par. 441). Under the Missouri statutory scheme, by contrast, if an establishment satisfies the 80/20 rule, *all* food items qualified under section 144.014 can be sold at the uniform food tax rate,

The Director also contends that the one-hour time limit is "arbitrary." Resp't Br. 22. But, as already explained, *supra* at 15-16, the one-hour period used by Krispy Kreme as a measuring device was a reasonable application of the statutory instruction that it determine the percentage of "food prepared by [its] establishment[s] for immediate consumption." Section 144.014.2. The resulting percentage of qualified food sold by Krispy Kreme's stores that meets the 80/20 rule was between 31.25 and 56.3 percent of their total retail sales, *see* L.F. 035-36 (¶ 8); Appellant Br. 4, 32, exceeding comfortably the 20-percent threshold. There is therefore no concern whatsoever that this Court would have to engage in any kind of fine parsing, having to determine whether doughnuts sold (and, therefore, consumed) shortly before or after the one-hour mark were "prepared for immediate consumption."

Next, the Director peddles a "slippery slope" argument, conjuring a parade of horribles that would have this Court forced to divine, "in future cases," that the time limit "should be 30 minutes, 5 minutes, or even 1 minute following preparation." Resp't Br. 23. This concern is similarly misplaced. No one would reasonably contend that food prepared one minute prior to consumption, or "'made to order' food," such as a hamburger or a burrito, Resp't Br. 23 & n.3, is not food that is being consumed without

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regardless of whether or not they had been "prepared for immediate consumption." Appellant Br. 31. n.15; *see also* Appellant Br. 8. The Director offers no response to this argument. *See* Resp't Br. 22.

any delay after preparation. In fact, Krispy Kreme expressly disclaimed any such argument. Appellant Br. 23.

To the extent the Director believes that a clear temporal line is desirable for the application of section 144.014's 80/20 rule, the Director can always promulgate an interpretative regulation setting forth such a bright-line requirement. Such a regulation would provide taxpayers with clear and transparent notice, and would enable the Missouri legislature to then determine whether such a bright-line rule effectuates the legislative intent. It is not proper, however, for the Director to surreptitiously alter the plain statutory meaning and her own published regulations, *see* Appellant Br. 38-39; *infra* at 25-26, effectively enacting a tax increase.

Similarly unavailing is the Director's criticism that Krispy Kreme's selection of a dozen doughnuts to determine when doughnuts are sold in bulk is "an arbitrary line." Resp't Br. 26. Again, this number is a reasonable application of the common-sense notion — accepted by the Commission, *see* L.F. 371 — that food purchased in bulk is not meant to be consumed immediately. *See* Appellant Br. 40. Indeed, the quantity adopted by Krispy Kreme for the purpose of analyzing its bulk sales is a more conservative estimate then the six-doughnut presumption adopted by other states for determining what constitutes sales of baked items not intended for immediate consumption. *See id.* at 41; *see also* Conn. Dep't of Revenue Servs., *Policy Statement 2002(2)* ¶ 400-646 (Feb. 22, 2002), *included at* A19; Mass. Dep't of Revenue, Reg. 830 CMR 64H.6.5(5)(e)3, *included at* A24; R.I. Div. of Taxation, Reg. SU09-59.A, *included at* A42; *see also* L.F.

026 (¶ 7) (indicating that Connecticut, Massachusetts, and Rhode Island have adopted a six-doughnut rule).

Parroting the Commission's reasoning, *see* L.F. 376, the Director contends that a customer buying a dozen doughnuts may be buying them "for a family, little league team, or church or office group," who will "eat them all within minutes." Resp't Br. 26. The Director, however, cites no evidence in support of this assertion; nor does the record provide any.[7] Whereas Krispy Kreme's dozen-doughnut presumption is based on the

[7] There is no support in the record for the Director's assertion that sales of doughnuts by the dozen are indistinguishable from sales of individual doughnuts, and that "the employees just pull the number based on the customer's order" and do not package the dozens of doughnuts any differently from individual sales. Resp't Br. 27-28. In any event, there is no such separate packaging requirement, and the Director's attempt to divine one from the Nevada Supreme Court's opinion in *Nevada v. McKesson Corp.*, 896 P.2d 1145 (Nev. 1995), misreads that decision. Contrary to the Director's claim, the bulk sales of purified water in *McKesson* were not "prepared … in gallons." Resp't Br. 27. Rather, the vending machines dispensing the purified water were "connect[ed] directly to municipal water lines, and then "dispense[d] *quantities of one gallon and greater* into containers *provided by the consumer*." *McKesson*, 896 P.2d at 1146 (emphasis added). To the extent this Court believes that further development of the record is needed on this issue, Krispy Kreme will introduce evidence demonstrating that the doughnuts sold by the dozen are being packaged separately, in pre-designed boxes, that Krispy Kreme's

considered judgment of other states (conservatively applied), the Director's contrary presumption is based on nothing more than naked speculation.[8]

V. KRISPY KREME'S INTERPRETATION OF SECTION 144.014 FURTHERS THE STATUTORY PURPOSE.

The Director asserts that Krispy Kreme's interpretation would frustrate section 144.014's purpose because the statute was not intended to apply to food purchases at a "fast food doughnut restaurant." *See* Resp't Br. 30-31.[9] This stands the statutory purpose on its head. As the Director acknowledges, the goal of section 144.014 is to provide a special food tax rate for consumers buying food products of the "'types … for which food stamps may be redeemed.'" Resp't Br. 30 (quoting section 144.014.2). The Director openly concedes that "doughnuts may be purchased at a grocery store with food stamps." Resp't Br. 31; *see also* L.F. 371. Because the statute is intended to benefit

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stores have special procedures for such sales, such as a "dozen" key on the registers, *see* L.F. 139, and that Krispy Kreme offers special pricing for doughnuts bought by the dozen.

[8] For reasons already explained, the Director's argument against Krispy Kreme's third basis for its refund claim similarly fails. *See supra* at 4 n.3, 10.

[9] As already explained, *see supra* at 14, Krispy Kreme's Missouri stores are not "fast food doughnut restaurants," but bakeries whose output is intended both for wholesale and for retail.

consumers purchasing a particular type of food products, "the type of vendor does not matter" for the purposes of section 144.014. L.F. 371. Indeed, section 144.014 expressly lists a variety of food establishments, such as "restaurant[s], fast food restaurant[s], delicatessen[s], eating house[s], or cafe[s]," that may sell qualifying food at the food tax rate, provided they meet the 80/20 rule. Thus, there is absolutely no merit in the Director's assertion that applying the same food tax rate to a bakery such as Krispy Kreme would somehow "stretch the interpretation of this statute beyond the plain language." Resp't Br. 31.[10]

The position advocated by Krispy Kreme would benefit consumers who purchase food stamp-eligible products. A bakery such as Krispy Kreme does not keep the tax that

[10] The Director's unsupported conjecture that some restaurants, such as "take and bake" stores, venues that "require[e] some assembly," or venues that "sell preserved and packaged food items," such as sauces, similarly founders upon the statute's plain meaning. The dictionary definition of "restaurant" is "an establishment where refreshments or meals may be procured by the public," *Webster's Third New International Dictionary* 1936 (1993), "a public eating house," *id.*, or "an establishment where meals are served to customers," *Random House Webster's Unabridged Dictionary* 1641 (2d ed. 2001); *see also Collins English Dictionary* (10th ed. 2009), *available at* http://dictionary.reference.com/browse /restaurant (defining "restaurant" as "a commercial establishment where meals are prepared and served to customers"). The Director's farfetched examples cannot be shoehorned into this definition.

it collects on its food sales. Instead, it remits all collected tax to the Director. The fundamental impact of this Court's decision, therefore, will be not on a company like Krispy Kreme, but on its consumers. If the Director's interpretation prevails, it would result in the imposition of a higher tax burden on individuals purchasing food stamp-eligible products, in direct contravention to section 144.014's intent to provide such individuals with the benefit of buying such food at a food tax rate.

This is not a hypothetical threat. As Krispy Kreme indicated, a well-known bakery chain store, with at least some locations in St. Louis, currently sells items similar to those sold by Krispy Kreme and charges the lower food sales tax rate on store-baked items. L.F. 038 (¶ 3). Under the Director's newly minted interpretation, however, this bakery chain — as well as all other bakeries operating in Missouri — would be required to increase the sales tax they charge their customers. This is why the *Amici* Associations, which represent both the retail and the wholesale baking industry, are urging this Court to reject the Director's unwarranted construction of section 144.014.

The Director's interpretation would create a visible disparity between consumers who purchase baked goods at a grocery or a convenience store and consumers who purchase identical goods directly from a bakery. The former would pay the lower sales tax prescribed by section 144.014 on qualified food items, while the latter would be subjected to the higher general sales tax. Nothing in the statutory scheme suggests that the Missouri legislature intended to foster such disparity, creating a disincentive for individuals shopping at retail bakeries. On the contrary, the broad listing of food

establishments that can be eligible for the food tax rate under section 144.014 (provided they meet the 80/20 rule) suggests that the legislature intended for this provision to have wide applicability, in order to benefit a large number of consumers. The Director's statutory construction would frustrate this legislative goal.

VI. CONTRARY TO THE DIRECTOR'S CHANGED POSITION, ANY PERCEIVED AMBIGUITY IN SECTION 144.014 SHOULD BE RESOLVED IN FAVOR OF KRISPY KREME.

In its briefing below, the Director consistently argued that "[s]ection 144.014 is *not an exemption statute*," but rather "is *a taxing statute* and is strictly construed in favor of the taxpayer and against the taxing authority." L.F. 299 (¶ 7) (emphasis added); *see also* L.F. 069 (¶ 10) (same). Ironically, however, the Director's construction of section 144.014 — which, she insisted, was made in favor of Krispy Kreme, as the taxpayer — resulted in the imposition of a higher sales tax rate. L.F. 298-99 (¶ 6).

Now, however, the Director has made a 180-degree turn, and asserts that section 144.014 "is in the nature of an exemption or exclusion," and "as such should be strictly construed [against the taxpayer] and certainly not expanded." Resp't Br. 14-15. Yet, the end result the Director seeks remains the same — the imposition of a higher tax rate upon Krispy Kreme's and similar baking establishments' customers.

The plain meaning of section 144.041 is clear, and supports Krispy Kreme's interpretation. *See supra* at 2-5. Regardless, by its plain terms section 144.014 is a tax imposition statute. Section 144.014.1 (mandating that "the tax *levied and imposed* … on

all retail sales of [qualified] food shall be at the rate of one percent") (emphasis added). The mere fact that section 144.014 happens to impose a lower tax rate than another statutory provision, section 144.020.1(1), is not a reason to stand the settled canon of statutory construction on its head and treat a statute that expressly "impose[s]" a tax as a tax-exemption provision. The Director should "not be permitted to blow both hot and cold," *Hall v. Brookshire*, 267 S.W.2d 627, 630 (Mo. banc 1954), and to shift her position at will, with the only consistent result being that consumers of food products must pay a higher rate.

VII. THE DIRECTOR'S POSITION IS FORECLOSED BY HER OWN EXISTING REGULATIONS, AND BY SECTION 32.053'S PROHIBITION ON CHANGING SUCH REGULATIONS RETROSPECTIVELY.

As Krispy Kreme demonstrated, *see* Appellant Br. 38-39, the Director's self-serving construction of section 144.014 conflicts with her own published interpretation of this statutory provision. In her regulations illustrating the operation of section 144.014, the Director expressly recognized that "cold salads and cold soft drinks" sold by a "[a] fast food restaurant" could count towards the 20-percent threshold of section 144.014. 12 CSR 10-110.990(3)(E), *included at* L.F. 041 and A17 (indicating that such a fast food restaurant could not satisfy the 80/20 rule if "[t]hese cold items represent [only] 10% of total gross receipts"); *see also* Appellant Br. 38. This example expressly illustrates that such food items — which are ready-to-eat but not necessarily prepared for consumption at once — do not constitute "items prepared for immediate consumption." *Id.*; *see also*

Mo. Dep't of Revenue, *Missouri Sales Tax Reduction on Food* (2009), http://dor.mo.gov/tax/business/sales/foodtax.htm, *included at* L.F. 42 and A18 (tax policy notice providing the same example).

This regulation cannot be reconciled with the Director's position in this litigation; yet the Director completely fails to address this conflict or to respond to Krispy Kreme's argument. The Director's silence is a telling confession that her position cannot be squared with her published regulations. Section 32.053, however, prohibits the Director from applying any "change in … interpretation" of existing regulations that affects "a particular class of person subject to such decision" retrospectively. Although the Director may change her existing regulations, she must do so through the formal notice-and-comment rulemaking procedure, *see* section 536.021, and may not simply discard regulations she now finds inconvenient by taking a contrary position in litigation. The Director's failure to abide by her own regulation constitutes an independent basis on which this Court may reverse the Commission's decision.

CONCLUSION

For the above-mentioned reasons, as well as those stated in Krispy Kreme's opening brief, this Court should reverse the Commission's erroneous conclusion that Krispy Kreme's stores do not satisfy section 144.014's 80/20 rule.

Respectfully submitted,

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RULE 84.06(C) CERTIFICATION

I hereby further certify that the foregoing brief complies with Rule 55.03 and with the limitations contained in Rule 84.06(b), in that it contains 7,062 words.

I hereby further certify that the labeled disk, simultaneously filed with the hard copies of the briefs, has been scanned for viruses and is virus-free.

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I hereby certify that on August 23, 2011, true copies of the foregoing document were mailed by US Postal Service and sent by e-mail to the following:

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