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Tax Policy

The Missouri Supreme Court ruled in 2016 that the expansive interpretation of the sales and use tax “manufacturing” exemption for electronic voice transmissions should not be followed. The Missouri legislature then enacted legislation to “pause” the ruling while it assessed its policy implications. In this article, Ryan LLC’s Randy Hilger discusses a Missouri Administrative Hearing Commission decision interpreting the 2016 ruling in a way that avoids the legislative pause.

Missouri ‘Suddenlink’ Decision Raises Questions Regarding Impact of 2016 and 2017 Legislation



BY RANDY HILGER

The Missouri Administrative Hearing Commission (“Commission”) issued a decision on May 19, 2017 in the case *Cebridge Acquisition LP and Friendship Cable of Arkansas Inc. v. Director of Revenue*, Case #13-1629 RS (both entities doing business as “Suddenlink”), which calls into question the impact specific to Missouri tax legislation passed in 2016 and 2017. At issue in *Suddenlink* was whether the taxpayers, which provide cable television, Internet access, and telephone service [through Voice over Internet Protocol (VoIP)], qualified for a Missouri sales and use tax exemption for pur-

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chases of manufacturing machinery and equipment.

Called into Question

In April 2016, the Missouri Supreme Court (“Court”) handed down a decision in *IBM v. Director of Revenue* [491 S.W.3d 535 (Mo. banc 2016)] (“*IBM*”) in which the Court ruled IBM’s customer Mastercard International did not qualify for a manufacturing exemption for computer hardware purchased for its global processing center in O’Fallon, Missouri. In ruling against IBM/Mastercard, the Court not only overturned a Commission decision in favor of the taxpayer but also called into question more than two decades of precedent involving the application of Missouri’s manufacturing machinery and equipment exemptions to processing ac-

tivities using computer technology. Specifically, the Court stated:

To the extent cases such as *Bell I* and *Bell II* suggest that an expansive interpretation of the word “manufacturing” is authorized by the “manufacturing” exemption, and to the extent that they hold that the electronic transfer of voices is itself manufacturing as that term is used in the exemption, they are no longer to be followed.

Suddenlink’s refund claim and appeal were based directly on the Court’s 2002 and 2005 *Southwestern Bell* decisions (referred to as *Bell I* and *Bell II* in the *IBM* decision), and the Commission, following the Court’s *IBM* decision, ruled against Suddenlink.

Taxpayer Protection Legislation

That the Commission ruled against Suddenlink, in light of the Court’s *IBM* decision, is not surprising. But immediately following the *IBM* decision, the Missouri Legislature passed taxpayer protection legislation, codified as Section 144.026 RSMo, which provides:

The director of revenue shall not send notice to any taxpayer under subsection 2 of section 144.021 regarding the decision in *IBM Corporation v. Director of Revenue*, Case No. 94999 (Mo. banc 2016) prior to August 28, 2017.

Designed to Delay Implementation

This legislation, in tandem with Subsection 2 of Section 144.021, which requires the Missouri Department of Revenue (“Department”) to notify taxpayers if the Department, the Commission, or a court issues a decision that changes application of the state’s sales tax exemptions if a reasonable person would not have ex-

pected the decision, was designed to delay implementation of the *IBM* decision, giving the Legislature time to analyze and deliberate the tax policy implications of the decision. Under 144.021, sellers are not required to follow the decision until they have received “notification” from the Department. New Section 144.026 was intended to hit a “pause button”—preventing the Department from issuing assessments or denying refund claims based on the *IBM* decision for a specific time period, while the Legislature received input from impacted industries, studied the issue, and developed a solution.

In its *Suddenlink* decision, the Commission analyzed the *IBM* decision, and concluded the Court’s ruling in *IBM* was not “unexpected” (even though the Court overruled the Commission’s original decision in favor of the taxpayer and called into question more than 20 years of decisions regarding the use of computer technology in producing and processing products and services), and as such, the taxpayer notification provisions in Sections 144.021 and 144.026 RSMo do not apply.

Extending the Pause Button

Although the Legislature did not resolve the matter during its 2017 session, which ended May 12, the Legislature again passed legislation, Senate Bill 49, which amended Section 144.026 extending the “pause button” another year until August 28, 2018.

If the Commission’s decision stands, it appears the Missouri Legislature’s 2016 and 2017 efforts to prohibit implementation of the Court’s *IBM* decision are moot, and taxpayers who relied on more than two decades of jurisprudence interpreting Missouri manufacturing exemptions may be subject to retroactive assessments or denied refund claims.

At press time, Suddenlink had not filed an appeal of the Commission’s decision.