

# THE PURPOSIVE APPROACH TO THE INTERPRETATION OF SALES TAX STATUTES

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*If sales tax statutes are to be interpreted rationally, courts must undertake a determination of legislative purpose. But a court which adopts a purposive approach is confronted with formidable problems. The author searches for the causes of defects in communication between courts and legislatures, and proposes an approach to judicial interpretation and legislative drafting which will provide a basis for rational construction of sales tax statutes.*

This article considers the practice and efficacy of the purposive approach to the interpretation of sales tax statutes. There is a severe lack of rational method in interpretation in this area, since the courts often either do not employ the purposive approach at all, or they do so inadequately. This, of course, is not unique to sales tax statutory construction. But what is somewhat unique is that legislators have too often enacted statutes with no ascertainable primary purpose to guide the courts. In this situation, method proves to be quite fruitless. What follows is an examination of the interrelationship between court and legislature and suggestion of instances in which institutional duties have been ignored and those in which these duties have been expertly performed.<sup>1</sup>

## I. MANUFACTURERS TAX

The case of *In re Taxes, Hawaiian Pineapple Co.*<sup>2</sup> serves as an interesting introduction to the intricacies of statutory interpretation.

The taxpayer operated a manufacturing plant in Honolulu where raw pineapple juice was boiled and hermetically sealed in tin cans.

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<sup>1</sup> This study adopts the purposive approach to statutory construction. To substantiate the principles of interpretation used, citation will often be made to Hart & Sacks, *The Legal Process; Basic Problems in the Making and Application of Law* 1306-1848 (tent. ed. 1958). It is assumed the reader is quite familiar with the work and conversant with the analysis supporting the conclusions found therein.

Not considered will be the role of the administrator in statutory construction, even though it is an important one in the tax area. There are two reasons. First, the courts give only slight recognition to administrative interpretation in deciding the cases studied. The courts rarely advance any presumption of correctness of administrative rulings. Secondly, in the cases examined, this writer feels the criticized decisions so clearly inadequate that administrative regulations consistent with the decisions should have been overturned in any event.

<sup>2</sup> 45 Haw. 167, 363 P.2d 990 (1961).

The taxpayer also hermetically sealed uncooked raw pineapple in tin cans and froze it until shipment. The tax commissioner contended that both processes fit within the meaning of "canning" as used in the statute.<sup>3</sup> The taxpayer argued that only the first process could be considered "canning," for the common and trade meanings of "canning" require sterilization by heat to kill the bacteria in the product so that it may be stored with no further concern for its preservation. The type of container is irrelevant, for after the "canning" process, a product may be sealed in a glass jar or bottle as well as a tin can.

The Supreme Court of Hawaii affirmed the ruling of the tax appeal court in favor of the taxpayer. The court began by quoting Sutherland on Statutory Construction: "[I]n the absence of a legislative intent to the contrary, commercial terms when used in a statute relating to trade or commerce are presumed to have been used in their trade or commercial meaning."<sup>4</sup> The court said that this rule of interpretation applied not only to statutes regulating commerce but also to taxation statutes when addressed to industry. Since the commissioner in his brief agreed with the taxpayer that "canning" in the trade sense required preservation by sterilization before disposition in containers, the court was well on its way to concluding the case. But the possibility that the legislature intended a meaning that might conflict with the trade understanding remained as a key issue.

The commissioner argued that the statute revealed a legislative

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<sup>3</sup> The statute read in pertinent part:

Imposition of tax. There is hereby levied and shall be assessed and collected annually privilege taxes against the persons on account of their business and other activities in this Territory measured by the application of rates against values, gross proceeds of sales or gross income, as the case may be, as follows:

A. Tax on manufacturers. (1) Upon every person engaging or continuing within this Territory in the business of manufacturing, compounding, canning, preserving, packing, milling, processing, refining or preparing for sale, profit or commercial use, either directly or through the activity of others, in whole or in part, any article or articles, substance or substances, commodity or commodities, the amount of such tax to be equal to the value of the articles, substances, or commodities, manufactured, compounded, canned, preserved, packed, milled, processed, refined or prepared for sale, as shown by the gross proceeds derived from the sale thereof by the manufacturer or person compounding or preparing the same (except as hereinafter provided) multiplied by the respective rates as follows:

Millers or processors of sugar, raw or refined, two and one-half per cent; canneries, two and one-half per cent; all manufacturers on whose gross income a tax is not otherwise levied in this chapter, one and one-half per cent.

Hawaii Rev. Laws § 5455 (1945), as amended by Haw. Sess. Laws 1947, act 3.

<sup>4</sup> 2 Sutherland, Statutory Construction 442 (3d ed. 1943).

intent to employ the ordinary and popular meaning, not that of the trade. He contended that this statute always spelled out special meanings and that, in defining wholesaler and jobber, the legislature specifically provided that the trade meaning should govern. Since the legislature failed to do either of these with "canning," the popular meaning must control. The court did not think this evidence of legislative intent compelling; it certainly was not sufficient to overcome the presumption arising from Sutherland's rule of construction, particularly since the legislature deleted the phrase "known to the trade as such" in defining wholesaler and jobber in 1957.<sup>5</sup> Evidently, the legislature eliminated the phrase because it realized that the terms would be so read without the language.

But, assuming that the commissioner was right about the legislature's intent, the court considered the ordinary meanings of "canning," and to this end it investigated dictionary and encyclopedia definitions. It concluded from these two sources together that the popular and trade meanings were the same. It found little merit in the commissioner's objection that encyclopedias should not be used for this purpose, but said that, even with dictionaries alone, taxpayer's contention as to the popular meaning was as reasonable as the commissioner's and in tax cases doubts are resolved in the taxpayer's favor.

The commissioner further argued, "That the legislature intended to impose the 2½% rate on pineapple products is expressed in Stand. Com. Rep. No. 85, 1935 Senate Journal 422-423."<sup>6</sup> The committee report stated:

This bill is the much publicized Gross Income Tax Bill, which proposes to levy a tax of 2¼% in a general way against those coming under the definition of "Retailers" and ¼ to 1% against those defined as "Wholesalers," at the same time levying the higher rate against sugar and pineapples immediately before such products enter into interstate or foreign commerce. It is described as a privilege tax,—a tax for the privilege of doing business in the Territory of Hawaii. This is the backbone of the administration's tax program.<sup>7</sup>

The evident argument of the commissioner was that this statutory purpose should influence the court to define words in such a way as to encompass the pineapple industry within the 2½ percent rate whenever possible. The court found this unconvincing because the report suggested no particular type of pineapple products to be included in the word "canned." Also, since canneries other than pineapple canneries processed on the island, if the legislature meant to heavily burden only

<sup>5</sup> Haw. Sess. Laws 1957, act 34.

<sup>6</sup> *In re Taxes Hawaiian Pineapple Co.*, *supra* note 2, at 183, 363 P.2d at 999.

<sup>7</sup> *Ibid.*

pineapples, it would "not be unreasonable"<sup>8</sup> to find more specific language than "canneries." Moreover, the tax administrators consistently levied on pineapple by-products at the lower manufacturer's rate. In sum, the court thought this evidence of legislative intent also too negligible to influence the application of the rule of construction and the consequent presumption of trade meaning.

The court went on to cite a recent federal case<sup>9</sup> which held that the Interstate Commerce Commission was not arbitrary or capricious when it ruled the word "canned" in the Commission's certificates of convenience did not authorize the transporting of frozen fruit products in hermetically sealed cans.

In construing the statute in the manner described above, the court employed inadequate tools of analysis. Its analysis should have commenced with a thorough review of the statute, attempting to identify any underlying, pervasive legislative purpose. This should give the proper direction and emphasis in interpretation. This is a difficult task, but there are a number of aids. The court should imagine itself in the role of the legislature and seek out the "mischief" that this provision sought to remedy. What motivated its enactment? To find the answer the court should analyze the prior state of the law, draw on general public knowledge of the prevalent "evils" of the time, consult the pronouncements of political and legislative leaders, and examine the internal legislative history.<sup>10</sup>

In this case, one could conclude that the purpose was simply to raise revenue—so all problems of interpretation ought to be resolved in such a way as to produce more income for the government. But this purpose carries little significance for two reasons. First, it may be argued that such a purpose should not be inferred in a jurisdiction that accepts the general rule that taxation statutes are to be construed strictly against the government.<sup>11</sup> Second, this broad statutory purpose pales in relation to purposes manifest in the specific section at issue. Canneries and sugar millers are set apart and are required to contribute much more than other manufacturers taxed at this level. Why did the legislature do this? What motivated the differentiation? The court can give a meaningful interpretation to the words of the section only by uncovering this motivation and construing the words in its context. This the court in *Hawaiian Pineapple* failed to do.

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<sup>8</sup> *Ibid.*

<sup>9</sup> *McDowall Transport v. United States*, 130 F. Supp. 681 (S.D. Fla. 1955).

<sup>10</sup> Hart & Sacks, *op. cit. supra* note 1, at 1414-17.

<sup>11</sup> See generally policies of clear statement and maxims of construction, *Id.* at 1412-13.

It may well have been that the legislature wished in some way to punish or retaliate against owners of the pineapple and sugar industries for their exploitation of Hawaiian resources. But the court must presume the legislature to be a body of reasonable men which enacts rational legislation, particularly in this case where no "due process" or "equal protection" issues were raised.<sup>12</sup> Thus, the court must identify the rational basis for the differentiation made in the statute. Three possibilities are readily apparent.

One rationale is that the legislature saw the canning and sugar industries as well established and assured of competing successfully in Hawaii and on mainland United States because of their proximity to and control over the products marketed. Thus, the higher tax rate could be passed on by these industries with no appreciable decline in sales. This is particularly significant with "canning" in light of the fact that "the pineapple industry is one of Hawaii's leading industries and the amount of canning done in the industry is immeasurably greater than that done by other canners in Hawaii. . . ."<sup>13</sup> It is not unlikely therefore that the legislature used the word "canning" as referring only to the pineapple industry and regarded Hawaiian pineapples as able to do well in competition on the mainland despite a small price rise. The Senate report reproduced above indicates that "canneries" meant pineapple canneries to the legislators.<sup>14</sup>

The court reacted to the commissioner's contention that only the pineapple industry was referred to by stating that if the legislature meant pineapple alone it could have so indicated. This is a penetrating argument in some instances,<sup>15</sup> but not here. The court should have faced the problem of explaining the differentiated rate. In fact, it was imperative to do so in order to avoid the implication that the higher rate was simply arbitrary and discriminatory. In so doing, it would have made apparent that when "canneries" is thought of as meaning pineapple canneries many sound reasons can be offered for the rate differential. But if "canneries" is interpreted blindly as referring to all canneries, no matter how obscure the others may be, the higher rate seems only a senseless fiat.

The court did not insist on precise terminology in another instance. The suggestion was made that since "canneries" may mean places where the business of canning is carried on, the 2½ percent cannery rate should apply to all manufacturing done in a cannery,

<sup>12</sup> *Id.* at 1415.

<sup>13</sup> *In re Taxes, Hawaiian Pineapple Co.*, *supra* note 2, at 183, 363 P.2d at 999.

<sup>14</sup> See text accompanying note 7 *supra*. See generally problems of use of legislative history, *id.* at 1242-84.

<sup>15</sup> See generally *id.* at 1220-22.

whether the products manufactured are "canned" or not. The court countered:

However, a construction producing that result would be wholly at variance with the overall purpose and patent general intent of the excise tax law to impose the tax in all cases on the income earner according to the nature of his particular business, and not on the basis of the place where it is conducted. Such intent undoubtedly might have been more-exactly expressed in fixing the rate for canning by the use of the term "canners" in place of "canneries," comparably to and consistently with the designation "millers or processors" in the preceding clause fixing the rate for sugar production. Notwithstanding this possible inexactness of terminology, we think it clear from a consideration of the framework and scheme of the entire statute, that the particular provisions under consideration must be construed to mean products manufactured in a plant which may be designated a "cannery" are not subject to the two and one-half per cent cannery rate unless they are "canned."<sup>16</sup>

Here the court evidenced the proper concern for the "overall purpose" and "general intent" of the statute which it omitted in concluding that "canneries" could not refer to pineapple canneries alone.

It is interesting to note that in 1957 the legislature changed the word "canneries" in the statute to "pineapple canneries (including canning of pineapple juice)."<sup>17</sup> This occurred after the period in question in the lawsuit, but should it have been completely ignored by the court? It is conceivable that the legislature thought one meaning should govern before 1957 and another thereafter. In such case, the amendment lacks significance. But in the absence of strong evidence to this effect, when logic leads to the same conclusion about meaning as is codified in a recent amendment, the amendment should at least take on significance as giving some assurance that reason is following the right path.

Another explanation for the higher rate may be found in the circumstance that the bulk of the products of these two industries is shipped out of Hawaii. Since Hawaii taxes at the retail and wholesale levels as well as the manufacturing level,<sup>18</sup> without the higher rate, sugar and pineapple products would be taxed only once at the same rate as other products and then sail out of reach of Hawaiian taxes while the other products for local consumption suffer two more levies. Thus, locally consumed goods would be taxed more heavily than pineapple and sugar. The legislature may have intended the higher rate to bring approximate equality in the taxation on manufactured prod-

<sup>16</sup> *In re Taxes Hawaiian Pineapple Co.*, *supra* note 2, at 175, 363 P.2d at 995.

<sup>17</sup> Haw. Sp. S.L. 1957, act 1.

<sup>18</sup> Haw. S.L. 1955, ch. 117.

ucts. The Standing Committee seems to imply this rationale when it says that there should be a levy of "the higher rate against sugar and pineapples immediately before such products enter into interstate or foreign commerce."<sup>19</sup>

A third possible legislative purpose might have been to enact something in the nature of a progressive corporate tax. It may be judicially noticed that pineapple and sugar are so stable economically that they could easily contribute more to the revenues than other relatively poor manufacturers, many of which may still need nurturing. Competitive conditions and ability to shift would then be irrelevant. This is a sensible rationale, but it is perhaps too unlike the common manner of taxing corporations to be readily attributed without express legislative recognition.<sup>20</sup> Thus, there are at least three plausible purposes that may have motivated the statutory provision at issue.

The court should next read the words in the provision at issue in light of the formulated purposes. The key words are "canned" and "canning." Any meaning attributed to these words must be one that the words will bear. Words cannot be construed to mean anything the interpreter wishes, even though a meaning the words will not bear seems most in tune with legislative purpose.<sup>21</sup> The dictionary assists in identifying meanings that words will bear. The court found in the dictionaries<sup>22</sup> that possible meanings were: (1) to preserve in cans

<sup>19</sup> See text accompanying note 7 *supra*.

<sup>20</sup> See generally Hart & Sacks, *op. cit. supra* note 1, at 1413.

<sup>21</sup> Hart & Sacks, *op. cit. supra* note 1, at 1225-26. For an example of a case in which the legislative purpose indicated a meaning the words would not bear, see *Olin Mathieson Chem. Corp. v. W. A. Johnson*, 257 N.C. 666, 127 S.E.2d 262 (1962). The clear purpose of the insecticide exemption was to keep costs down on chemicals used in farming. It seems that in the *Mathieson* case the chemical in issue impeded plant growth and thereby kept eggs from being laid on the plant. The court felt it could not bring this chemical within the meaning of "insecticides." What if eggs were laid on plants treated with plant growth inhibitor but were unable to hatch because of the arrested plant growth? Could it then be considered an insecticide? The North Carolina statute was amended to include "herbicide" within the exemptions allowed by the provision at issue in this case. Can "herbicide" bear a meaning that would include growth inhibitors as well as plant destroyers?

<sup>22</sup> The Oxford English Dictionary (1933) defines "canning" as:

The preserving of meat, fish, fruit, etc., by sealing up in cans or tins; tinning.

From Webster's New International Dictionary (2d ed.) 1934, are the following:

can (kan), v.t.; CANNED (kand); CANNING. 1. To put in a can or cans;

to preserve by putting in sealed cans or jars.

canned (kand), adj. 1. Preserved in cans, as canned goods.

canning (kan'ing), n. The process or business of sealing food in cans or jars, esp. for commercial distribution.

The third reference is to Funk & Wagnalls' New Standard Dictionary (1956) which defines "canning" as: "The act, process, or business of preserving fruits, vegetables, or

by cooking and sealing, or (2) to put or seal in cans or jars. Encyclopedias and trade terminology also aid in determining meaning. Both of these indicated that "canning," in technical usage, meant preserving in cans with heat sterilization. Maxims of construction supply a third source.<sup>23</sup> One such maxim reads, "every word and clause must be given effect," and another, "words are to be interpreted according to the proper grammatical effect of their arrangement within the statute."<sup>24</sup> The taxing section encompasses both "canning" and "preserving" ("canned" and "preserved"). If canning meant nothing other than preserving in cans by cooking, as the taxpayer contended and the court decided, why was the word "canning" even inserted? If every word is to be given effect, certainly "canning" must refer to something other than just a process of preservation. The other meaning could well be the sealing of products in cans.<sup>25</sup> In any event, this indicates that the words will bear the meaning sought by the commissioner.

From this analysis, two meanings seem possible. But only one is totally consistent with any of the three possible purposes—that which includes anything sealed in a can.

If with the first formulation the court adheres to the legislative assumption that pineapple canneries and sugar millers can shift the tax and still readily compete, it follows that frozen pineapple juice should be regarded as able to sell as well with a slightly higher price forced upon it by the statute. Therefore, the meaning of "canning" should prevail which brings the frozen juice under the higher rate. However, it may be thought that the court must analyze competitive conditions for each product or at least for the industry as a whole, for the true legislative purpose was to tax more heavily, provided that competitive conditions were such that the shifting could take place. The proviso stems from an overriding purpose to keep the two industries economically sound. But such a formulation is not appealing. It produces the type of litigation the anti-trust laws have forced on the federal courts. The judicial process is not well suited for fact finding of this scope.<sup>26</sup> Courts should be hesitant to make this type of determination unless conditions have changed to such a degree that judicial notice may be employed. Otherwise, the court should assume condi-

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meats, by partial cooking or other process, and hermetically sealing in tin cans, glass jars, etc."

*In re Taxes Hawaiian Pineapple Co.*, *supra* note 2, at 175-76, 363 P.2d at 1000.

<sup>23</sup> Hart & Sacks, *op. cit. supra* note 1, at 1220-22.

<sup>24</sup> Llewellyn, "Remarks on the Theory of Appellate Decision and the Rules or Canons About How Statutes Are To Be Construed," 3 Vand. L. Rev. 395 (1950).

<sup>25</sup> It can be argued that the word "preserving" refers to such processes as the drying and glazing of fruit while "canning" is used to cover the case of sterilization by heat.

<sup>26</sup> See *Standard Oil Co. v. United States*, 337 U.S. 293 (1949).



tions similar to those upon which the legislation is premised and leave it to the legislature to change the law when the premise is invalid. The interpretation of a statute should not be based on something as variable and complex as competitive conditions unless this is clearly the legislative mandate.<sup>27</sup>

But if a formulation with a proviso is preferred, the next step is to select the one primary purpose according to the guidelines set out above.<sup>28</sup> The court may well decide that this first discovered purpose will prove irrelevant, leaving the words to be construed in light of the other suggested purposes. On the other hand, if this first formulation of legislative purpose does prove primary, it will then become necessary to delve into the files of the fruit industry in order to determine the fate of these tins of pineapple.

The higher rate best complies with the thrust of the second purpose. Frozen pineapple juice in cans is just as much an export product as other pineapple products. It also would escape its fair share of the total tax burden if not taxed at the higher rate.

Similarly, frozen pineapple should be taxed at the higher rate if the third tentative purpose is to be effectuated. The progressive tax would be too easily evaded if it were only necessary to change the method of preservation.

Thus the court seemingly chose a meaning of "canning" that did not best comply with discernible legislative purpose. The purposive meaning is not forced. It is found in dictionaries alongside the alternative meaning. It accords with maxims of construction. However, the significant point is not that a wrong result may have been reached but that the approach was incorrect. The court erred in not performing its institutional duty to identify purpose where it is ascertainable.<sup>29</sup> Without this foundation in interpretation, the dictionary can be of little assistance.

## II. RETAIL SALES TAX—THE MANUFACTURING EXEMPTION

### A. *Background*

Economists have advocated for many years that the retail sales taxes of the states should be levied only on sales for final personal consumption.<sup>30</sup> Some of the reasons given are:

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<sup>27</sup> See generally Hart & Sacks, *op. cit. supra* note 1, at 398, 1413.

<sup>28</sup> See text accompanying note 10 *supra*.

<sup>29</sup> If necessary, further evidence of the court's lack of appreciation of the concept of purpose can be found in its citation of the *McDowall* case, *supra* note 9, where the purpose behind the statute interpreted by the ICC was so patently different from that in this case that the result in the former case was not relevant.

<sup>30</sup> See, e.g., Jacoby, *Retail Sales Taxation* (1938); Due, *Sales Taxation* (1957); Oster, *State Retail Sales Taxation* (1957); Studenski, *Characteristics, Developments and Present Status of Consumption Taxes*, 8 *Law and Contemp. Prob.* 417 (1941).

1. The theoretical basis for the retail sales tax is that of a consumption tax which requires the tax burden to be distributed in proportion to final consumption expenditures. Even assuming shifting, this distribution cannot be achieved if earlier-than-ultimate sales are also taxed because of the variation in the number of taxable transactions through which products travel before reaching the ultimate consumer.

2. If producer's goods are taxed, labor intensive production methods would be more advantageous than capital intensive methods. This would impair modernization and investment.

3. With shifting, not only the amount of the tax at the early stage is passed on to the final consumer but also a percentage mark-up on it. This is known as pyramiding and, of course, becomes more serious the farther from final consumption the first tax is levied.

4. If there is multiple stage taxation, a greater burden is placed on non-integrated firms. This stimulates combination.

Some of these reasons may be spurious. That is, it may not be an evil to burden the capital sector if this is thought to offset capital favoritism elsewhere. Also, shifting may not be significant enough to cause concern about unequal tax burdens and pyramiding. Most importantly, the state retail sales tax may perhaps not be best explained in terms of consumption taxation considering the widespread exemption of services and the taxation of producer goods. But the state legislatures appear to be influenced, in varying degrees, by the economic "evils" outlined above. No state taxes sales of articles for resale. All exempt some producer goods, but these "manufacturing" exemptions take diverse forms.

The "physical ingredients" rule is the most widespread of the manufacturing exemptions. In light of the economic theory of taxing only final personal consumption, this test seems unsound. It is sophistry not to tax a manufacturer of copper wire on purchases of copper on the ground that to do so would cause unequal tax burdens and pyramiding when at the same time he is taxed on purchases of machinery or fuel. But the use of this test is justified usually in terms of its administrative ease.<sup>31</sup> Undoubtedly revenue considerations also prompt its enactment.<sup>32</sup> It is conceivable that this test actually evidences a rejection of some of the theory outlined above. That is, the legislature may be adhering to theories that require taxing investment

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<sup>31</sup> Due, *op. cit. supra* note 30, at 298; Redlich, "Sales Taxes and the Resale Exemption in the Manufacture and/or Distribution of Personal Property," 9 Tax L. Rev. 435 (1954).

<sup>32</sup> Due, *op. cit. supra* note 30, at 299.

goods; the "ingredients" rule serves only as a buffer against the evils associated with a turnover tax.

A second type of manufacturing exemption excludes transfers of products "dissipated" in the process of manufacturing. The "physical ingredients" rule always accompanies this test. In the case of the copper wire manufacturer, fuel consumed would be exempt if used in the process of manufacturing. But what type of "dissipation" or "consumption" does the test contemplate? Would the test exclude, for example, machinery? Many states adhere to the notion that to be "consumed" the product must not have a useful life of more than one year. Other states always tax machinery without reference to useful life.<sup>33</sup> This test, more than the "physical ingredients" test, suggests a sympathetic treatment of the capital sector which is, however, tempered by revenue and administrative considerations. It more fully complies with the notion of taxing only the final personal consumer than the "ingredients" rule, but it raises more severe problems of definition.

The advocates of taxing only final personal consumption no doubt influenced the few legislatures that have enacted the "used in manufacturing" exemption. This exemption is more consistent with the economic theory; but it still stops short of the theoretical ideal since it does not exclude all sales to producers. The term "used in manufacturing" is rather obtuse phraseology to express a purpose to exempt all such sales. The West Virginia provision exempting all sales of materials to persons "in the business of manufacturing"<sup>34</sup> would seem more appropriate. Moreover, sales of capital goods to distributors are not exempt as theory would dictate. It is not easy to explain this "almost but not quite" compliance with theories of ultimate personal consumption found in the "used in manufacturing" provisions.<sup>35</sup>

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<sup>33</sup> Redlich, *supra* note 31.

<sup>34</sup> W. Va. Code Ann. § 999(2)(6) (1961).

<sup>35</sup> The limitation to "used in manufacturing" is justified by Professor Due in this way:

Many commodities, such as automobiles, are used for both production and consumption purposes, often by the same persons. If all commodities which are utilized as producers goods in any instances are exempted completely (regardless of use in particular cases), numerous consumer purchases will escape tax. If on the other hand all purchases by firms for business use are exempted on a basis conditional upon use, the task of checking upon actual use is a very difficult one in many instances. Small firms will buy tax free under license goods which the owners actually employ for consumption purposes.

Due, "The Nature and Structure of Sales Taxation," 9 Vand. L. Rev. 123, 133 (1956).

The failure to consider distributors might be based on:

[T]he view that the selling price of a distributor is governed principally by the

If all goods sold to producers are not exempt under the "used in manufacturing" rubric, where should the line be drawn? The most sensible distinction separates manufacturing from administration, acquisition, distribution, and selling. This distinction can readily be attributed to the legislature.<sup>36</sup> It is workable, although as will be seen it may cause much administrative difficulty.

Because of the cross-purposes alive in the "manufacturing" exemptions, the legislature has made statutory interpretation a difficult task for the courts. It often seems that there is no recourse but to flip through the dictionary in search of the "ordinary" meanings of words. But some courts have wandered aimlessly through interpretation problems when the purposive approach would have given significant guidance.

### B. *Judicial Floundering*

In *Bedford v. Colorado Fuel & Iron Corp.*,<sup>37</sup> the taxpayer, a producer of steel and coal, contended that numerous articles, such as feed for mine mules, refractories in steel furnaces, repair tools, and trucks should not bear a tax under the statute<sup>38</sup> since they "enter into the process of" manufacturing or compounding. The trial court held, "such items of tangible personal property as are directly and proximately used in, and necessary for, the purposes of manufacture by the company, as well as those which become an ingredient or com-

cost of the product he sells rather than by the cost of the other items he may buy. . . . These costs on capital items, it is felt are not an important component of the retail price as is, for example, the cost of the ingredients or the cost of the machine which did the fabricating. In this view the selling prices of most distributors are based on traditional mark-ups. . . . The imposition of a sales tax on these purchases by wholesalers and retailers, therefore, is not reflected in the selling prices.

Redlich, *supra* note 31, at 448. Revenue considerations and a failure to fully understand the theory involved must also play an instrumental role in the enactment of these provisions.

<sup>36</sup> Note, "The Manufacturers Exemption in the Pennsylvania Sales and Use Tax," 58 Dick. L. Rev. 152 (1956).

<sup>37</sup> 102 Colo. 538, 81 P.2d 752 (1938).

<sup>38</sup> The statutory provision at issue read:

Sales to and purchases of tangible personal property by a person engaged in the business of manufacturing, compounding or furnishing for sale, profit or use, any article, substance or commodity, which tangible personal property enters into the processing of, or becomes an ingredient or component part of the product or service which is manufactured, compounded or furnished and the container, label, or the furnishing shipping case thereof, shall be deemed to be wholesale sales and shall be exempt from taxation under [this act].

Colo. Rev. Stat. Ann. ch. 138-5-2 (1964).

ponent part of the product manufactured,"<sup>39</sup> are exempt. Under this test, some non-ingredients escaped taxation, but the lower court still allowed a levy on machinery and equipment.

The Supreme Court of Colorado commenced its review in good fashion. It sought out legislative "intent," and it recognized that the legislature probably wished to avoid pyramiding and double taxation on the final product offered for resale to the consumer. Yet, there is a hint that the court thought the legislature wanted to avoid these "evils" only where ingredients were involved. The court noted that the legislature levied the tax on retail sales, which term does not include sales for resale. It then concluded:

The ultimate consumer of all articles purchased and used by a manufacturer in its manufacturing operations is the manufacturer and upon the basis of the definitions alone the manufacturer would be liable for the tax on all such items. It is definitely evident, however, that the legislature had well in mind that in the ordinary course of our complex industrial and commercial systems many articles and commodities are used and consumed by processors and manufacturers for later resale in altered form.<sup>40</sup>

Thus, since sales for resale were not taxed, the "ingredient" exemption was required where, according to the court, there is technically no resale, but where realistically, a transfer amounting to the same thing occurs. This justification for the manufacturing exemption does not apply to the "dissipation" or "used in manufacturing" exemptions because there is no physical transfer. It is conceivable that the court either did not see the possible economic "evils" in taxation of non-ingredient producer goods or thought the legislature did not see them.

Perhaps with this notion of purpose, the court then considered dictionary meanings of the phrase "enters into." The usual definition was: "to form a constituent or ingredient part of (as lead enters into the composition of pewter)."<sup>41</sup> It then found the dictionary definition of "processing": "a series of actions, motions or occurrences; progressive act or continuous operation or treatment; a series of operations leading to some result; as a process of manufacture."<sup>42</sup> At this point, the court overturned the lower court's exemption of non-ingredients by concluding: "that to enter into the processing of an article, tangible personal property must of necessity become a constituent part of such final product in the series of continuous operations and treatment lead-

<sup>39</sup> *Bedford v. Colorado Fuel & Iron Corp.*, *supra* note 37, at 542, 81 P.2d at 754.

<sup>40</sup> *Id.* at 543-34, 81 P.2d at 755.

<sup>41</sup> *Id.* at 546, 81 P.2d at 755-6.

<sup>42</sup> *Ibid.*

ing to the result."<sup>43</sup> The court felt there was legislative support for this conclusion due to the unfairness that would result from exempting substantially all property purchased by a manufacturer when distributors would still be liable on capital goods used in the conduct of their businesses.<sup>44</sup> Moreover, the court thought the administrative simplicity of the "physical ingredient" rule argued against a legislative purpose which would involve courts and administrators in the vagaries of the "used in manufacturing" test.

As in *Hawaiian Pineapple*, the court refused to concentrate on uncovering the likely legislative purpose. In this case, two tools of analysis would have led to purpose. The first, and most basic, was the pattern of the statute. The court's conclusion requires a narrowing<sup>45</sup> of "enters into the processing of" to the extent that that phrase repeats the "physical ingredient" phrase that follows.<sup>46</sup> The use of the disjunctive makes it extremely improbable that the legislature left this alternative to the courts, particularly when the word "and" could easily have been used instead. Thus, the pattern suggests a legislative purpose to exempt beyond the "physical ingredients" rule. Secondly, an attempt by the legislature to extend the test beyond "physical ingredients" is quite likely if viewed in light of sales tax economics. The court should have placed greater emphasis on the economic "evils" the legislature might mitigate with a "used in manufacturing" exemption. Thus, the court forced a statutory construction contrary to the result that could be easily reached by using the right tools. This could be justified only if some all-important legislative cross-purpose required it,<sup>47</sup> but certainly, nothing of such magnitude seemed to exist in this case.

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<sup>43</sup> *Id.* at 547, 81 P.2d at 756.

<sup>44</sup> But see Redlich, note 35 *supra*.

<sup>45</sup> Note that the court did not speak in terms of narrowing a broad phrase. This may have been an acceptable approach if purpose so dictated. It felt that the words required the "physical ingredients" test in themselves and the dictionaries would allow no broader construction. Actually, it can be argued here that the words could not bear the attributed meaning, in which case this meaning could never prevail. See text accompanying note 22, *supra*.

<sup>46</sup> The court spoke against the redundancy point in this way:

The solicitude of the legislature to make clear that in "processing," to be tax exempt tangible personal property must actually and factually enter into the subject matter transformed in the process, as in manufacturing proper it is required to become a constituent of the product, logically accounts for the circumstance that the two distinctive clauses under examination were drawn to effect a substantially similar result and dispels any suggestion that the clauses are redundant.

*Bedford v. Colorado Coal & Iron Corp.*, *supra* note 37, at 550, 81 P.2d at 757. There was no warrant in purpose for this extensive grammatical distortion.

<sup>47</sup> Hart & Sacks, *op. cit. supra* note 1, at 1412.

The only real question should have been the extent of the exemption beyond "physical ingredients." Probably all sales to manufacturers should not be exempt.<sup>48</sup> The administrative difficulty of the "used in manufacturing" test perhaps warranted some hesitation in reading it into the statute. However, the administrative difficulties of the "dissipation" test do not seem great enough to infer a supervening cross-purpose to defeat any extension whatsoever. The significant point is simply that the legislature could not have more clearly expressed a purpose to further comply with prevalent economic theory of sales taxation unless it actually spelled out such purpose in print. The court's *tour de force* completely frustrated this effort.

It is appropriate to discuss briefly two other arguments employed by the court to support its position. The court pointed to a section of the taxing statute which exempted sales of electricity, coal and gas from the sales tax. This provision might be appropriate for gas and electricity because they might not be considered tangible personal property. But to exempt coal used in manufacturing would just duplicate the provision at issue if the taxpayer's reading of it was correct. Obviously, other explanations for the inclusion of coal can be offered; *e.g.*, as a forceful fuel lobby, and the uncertainty of what the courts would do with the provision at issue. The court also referred to the fact that although the treasurer construed the sales tax act to exempt nothing but "physical ingredients," the legislature reenacted it without making any change. Does this argument have any force? If so, does it apply to general tax codes?<sup>49</sup>

Unlike the Colorado Supreme Court in the *Bedford* case, the Alabama Supreme Court has often construed its tax statute in the spirit of the "final consumer" theory of sales taxation, even though it never has given theory express recognition.

The taxpayer in *State v. Southern Kraft Corp.*<sup>50</sup> manufactured paper and pulp. The commissioner assessed taxpayer for its purchases of salt cake, sulphur, lime, starch, hydrate of lime and chlorine used in the process of manufacture. The taxpayer protested on the ground that the sales tax exempted "physical ingredients."<sup>51</sup> The evidence showed that the chemicals were used to produce a cooking liquor in which wood chips were boiled to make pulp. Through chemical reaction, 6/10 of 1 percent of the salt cake remained as an ingredient of the pulp and went into the paper; 2/100 of 1 percent or less

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<sup>48</sup> See text accompanying note 33, *supra*.

<sup>49</sup> Hart & Sacks, *op. cit. supra* note 1, at 1401-05.

<sup>50</sup> 243 Ala. 223, 8 So. 2d 886 (1942).

<sup>51</sup> Ala. Code, tit. 51, § 787(d) (1940).

of the hydrate of lime and chlorine became an ingredient of the pulp and went into the paper; and 1 percent of the sulphur remained in the paper. The commissioner contended that the dominant purpose in the use of these chemicals was to form the cooking liquor and the percentage of chemicals that remained in the paper was due to mere happenstance. The court said:

To adopt the "dominant purpose" thought or the percentage basis for computing the tax would be tantamount to writing into the statute something the legislature did not, and would be judicial legislation.<sup>52</sup>

The court, in holding for the taxpayer, seemed primarily interested in the fact that the chemicals, on analysis, were detectable in the finished product.<sup>53</sup>

In *Alabama-Georgia Syrup Co. v. State*,<sup>54</sup> the taxpayer processed sugar which it sold in fiber boxes to wholesalers (the immediate containers for the syrup were bottles and cans). The statute involved defined as wholesale sales purchases of "the furnished container or label thereof"<sup>55</sup> of manufactured or compounded products. The commissioner levied on the purchase of the fiber boxes by the taxpayer on the grounds that they were only for taxpayer's convenience in shipping and not for use as containers of the syrup. The final consumer buys the syrup in the cans or bottles so that the fiber boxes cannot fit within the phrase "furnished container." The court held for the taxpayer, stating:

There is nothing in the statute which says the product shall have actual contact with the container. Nor does the statute say that when there is more than one container of the product, only the inner container is to be excluded from the tax. As it is not denied that the fiber boxes are "furnished," they seem to qualify for exclusion from the tax under the statute.<sup>56</sup>

Reels and spools necessary to make cables marketable have been held to fall within the term "container," though the Alabama Supreme Court recognized this to be an unusual meaning of the word.<sup>57</sup>

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<sup>52</sup> *State v. Southern Kraft Corp.*, *supra* note 50, at 227, 8 So. 2d at 890.

<sup>53</sup> Compare *Smith Oil & Refining Co. v. Department of Finance*, 371 Ill. 405, 21 N.E.2d 292 (1939).

<sup>54</sup> 253 Ala. 49, 42 So. 2d 292 (1949).

<sup>55</sup> Ala. Code, tit. 51, § 787(d) (1940).

<sup>56</sup> *Alabama-Georgia Syrup Co. v. State*, *supra* note 54, at 53, 42 So. 2d at 800.

<sup>57</sup> *State v. Reynolds Metal Co.*, 263 Ala. 657, 83 So. 2d 709 (1955). For another instance of liberal construction of the "furnished container" provision, see *State v. Taylor*, 262 Ala. 639, 80 So. 2d 618 (1954).



In *State v. Wertheimer Bag Co.*,<sup>58</sup> the commissioner argued that only the farmer prepares agricultural products for market within the meaning of the exemption at issue<sup>59</sup> so that when the bag company sells bags to peanut hullers, who separate the kernel from the hull and bag the hulled peanuts for sale to confectioners, the company is liable. The court investigated legislative history of the section and concluded that the legislature would have specified farmers if that was the only group it intended to exempt. Peanuts are an agricultural commodity and "preparing them for market may well include shelling, since they are not marketable in the shells or pods."<sup>60</sup> The court also held taxpayer not liable for sales of bags to nursery owners who use them to hold soil around the roots of stock for shipment. The court found in dictionaries and other cases that the term agriculture could include horticulture and that there would be no purpose served in distinguishing horticulture from agriculture in this instance, even though it may not fit the "ordinary" meaning of the word. Thus the Alabama court has often construed liberally with the result that no tax is paid before goods reach the final consumer.

But the Alabama judicial attitude seems quite different in construing the statutory provision which exempts, "machines used in mining, quarrying, compounding, processing, and manufacturing of tangible personal property . . ."<sup>61</sup> The Alabama court narrowed this statutory language to exempt only machines used directly on the production line.<sup>62</sup> Machines used to remove ash from furnaces on the production line; machines used to repair, inspect or maintain production line components;<sup>63</sup> machines used to transport goods from one area of a plant to another<sup>64</sup>—all have fallen outside the exemption.<sup>65</sup>

Why this concern for the production line? The court may reasonably differentiate between manufacturing, administration, distribution, etc., since the provision is too awkward and obtuse to suggest a legis-

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<sup>58</sup> 253 Ala. 124, 43 So. 2d 824 (1949).

<sup>59</sup> Ala. Code tit. 51, § 755(i) (1940):

"The gross proceeds of the sale, or sales, of . . . bags . . . used in preparing agricultural products, dairy products, grove or garden products for market . . . when such . . . bags . . . are to be sold or furnished by the seller of the products contained therein to the purchaser of such products."

<sup>60</sup> *State v. Wertheimer Bag Co.*, *supra* note 58, at 127, 43 So. 2d at 827.

<sup>61</sup> Ala. Code, tit. 51, § 755(p) (1940).

<sup>62</sup> *State v. Calumet & Hecla Consol. Copper*, 259 Ala. 225, 66 So. 2d 726 (1953).

<sup>63</sup> *Alabama Power Co. v. State*, 267 Ala. 617, 103 So. 2d 780 (1958).

<sup>64</sup> *Alabama-Georgia Syrup Co. v. State*, *supra* note 54.

<sup>65</sup> See also *Southern Natural Gas Co. v. State*, 261 Ala. 222, 73 So. 2d 731 (1953). For a case which stresses the "production line" criterion and then stretches it beyond recognition, see *State v. Try-Me Bottling Co.*, 257 Ala. 128, 57 So. 2d 537 (1952).

lative purpose to follow economic theory so far as to exclude purchases of all machines for any use by the producer. But within the "compounding, processing, and manufacturing" categories, why does the court create further limitations with "production line" analysis? Unlike the interpretation given the provisions discussed earlier, the Alabama judicial approach here seems out of tune with the "final consumer" theory of sales taxation. One may try to explain this by pointing out that the "machines" provision is an express exemption while the "furnished container" and "ingredient" provisions are part of the definition of wholesale sale. Courts generally say they construe exemptions strictly against the taxpayer. This explanation answers little since the "bags in agriculture" provision of the *Wertheimer* case was also an exemption. Moreover, the Alabama Supreme Court tempered the general rule when it said in *State v. Calumet & Hecla Consol. Copper*,<sup>66</sup> concerning a "machine" case:

It is true that exemption statutes are to be strictly construed in favor of the taxing authority . . . but the court will indulge in no strained construction to give effect to this rule where a fair interpretation of the legislative intent may lead to a contrary construction.<sup>67</sup>

One could conclude that from a theoretical viewpoint the court is simply inconsistent. It may be as simple as that since the court never expressly speaks of economic theory and could well contradict itself on a level of analysis it never considered. In defense of the court, it could be asserted that the legislative directive to avoid pyramiding, etc., came through clearly enough in the "furnished container," "ingredient," and "agriculture" cases to warrant its prevailing over the cross-purpose of raising adequate revenue; but the same directive could not prevail over the revenue raising interest where heavy machinery was at issue and the taxes at stake more substantial. Such reasoning is not convincing because it is questionable that the revenue involved in the former type of case totaled less than in the latter because in the former there was greater frequency of purchases. More importantly, the "machines" exemption indicated that the legislature proposed to follow the economic theory of "final consumption" within the "compounding, processing, manufacturing" rubric; any narrowing of the meanings of these words defeated this purpose, particularly where large sums were involved and the evils of pyramiding, and the like, more apparent. The legislature wished to raise revenue, but it also made clear a desire to avoid "evils" arising from its tax measure, and the court should assist by giving effect to the reasonable implications of the words

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<sup>66</sup> *Supra* note 62.

<sup>67</sup> *Id.* at 232, 66 So. 2d at 729-30.

"compounding, processing, or manufacturing" in light of the legislative objective. This may not warrant extremely liberal construction, but it does argue against narrowing.

Thus, this court also failed to delve deeply enough to uncover legislative purpose. If it had, its decisions would not have been inconsistent, and it would have construed the "machine" exemption in the same open spirit that characterized its "ingredients" and "furnished container" decisions.

The Supreme Court of Michigan<sup>68</sup> has often liberally construed its "used in industrial processing" provision.<sup>69</sup> The court has been restrictive only in differentiating between such operations as "industrial processing," administration, and distribution.<sup>70</sup> The cases do not speak of the production line.

The case of *Minnaert, d.b.a. Minnaert Constr. Co. v. Dep't of Revenue*,<sup>71</sup> demonstrates this. Here the taxpayer contracted with the White Pine Copper Company to construct dams and ponds which served to separate waste copper tailings from the water that ran through the copper mill. The water could then be reused. The taxpayer bought heavy earth moving equipment for the exclusive purpose of fulfilling this contract. The court thought the disposition of waste to be "an essential part of White Pine's process of manufacture"<sup>72</sup> and exempted the taxpayer from the use tax on the earth moving equipment. It spoke of the equipment as permitting a more "economical" manufacturing operation. Obviously, this decision is extreme.<sup>73</sup> The

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<sup>68</sup> The Michigan lower courts have been restrictive. See, e.g., *Dean Chemicals, Inc. v. Dep't of Rev., P-H State and Local Tax Serv.* ¶ 23004; *Smith Co. v. Dep't of Rev., P-H State and Local Tax Serv.* ¶ 23545.

<sup>69</sup> Sec. 4a. No person subject to tax under this act need include in the amount of his gross proceeds used for the computation of the tax any sales of tangible personal property:

(g) To persons for use or consumption in industrial processing: Provided, that the term 'industrial processing' shall not be deemed to include tangible personal property permanently affixed and becoming a structural part of real estate.

*Mich. Stat. Ann.* § 7.525 (1960).

<sup>70</sup> See, e.g., *Bay Bottled Gas Co. v. Dep't of Revenue*, 334 Mich. 326, 74 N.W.2d 37 (1955).

<sup>71</sup> 366 Mich. 117, 113 N.W.2d 868 (1962). The statute at issue in this case was the use tax statute. This factor seems insignificant in this situation.

<sup>72</sup> *Id.* at 124, 113 N.W.2d at 871.

<sup>73</sup> Indeed, it may be argued that the case went too far in that the legislative purpose, while warranting liberal construction, did not warrant extension to the point of distortion of the term "used in industrial processing" which may be true in this decision. For another case of extremism, see *State Bd. of Equalization v. Standard Oil & Gas Co.*, 51 Wyo. 237, 65 P.2d 1095 (1937), where the court exempted as a service "used in the production or entering into the processing of" oil the purchase of transportation services which moved

dams were far removed from the reduction of ore to pure copper even if "essential" to it, and the earth moving machinery was even farther removed. A test based on economy of operation is quite a maverick. This treatment of waste removal can be contrasted with that of the Alabama case which would not exempt machinery used to remove ashes from furnaces in the production line.<sup>74</sup>

Another example of this court's attitude can be found in *Michigan Allied Dairy Ass'n v. Board of Tax Administration*.<sup>75</sup> In that case, one of the issues was whether "milk bottles and cans purchased by milk processors are used in industrial processing, or whether they are only convenient containers in which to deliver the contents."<sup>76</sup> The court found that the bottles and cans contained the milk while it underwent refrigeration to preserve it from contamination by bacteria before delivery to customers. The court held that since the refrigeration kept the milk suitable for marketing, it thereby became part of the industrial process even though there was no processing in the sense of adding to or changing the product.<sup>77</sup> The court next considered, "whether the exemption should apply inasmuch as the milk bottles and cans are also used as delivery containers, the latter use not being industrial processing."<sup>78</sup> The court said:

Where an article has more than one use, one or more (but not all) of which are within the agricultural producing or industrial processing exemptions, the legislature could have provided that the portion of the value of the article representing its nonexempt uses should bear the tax, but it has not done so.<sup>79</sup>

In another aspect of the case, the court concluded that cans used by farmers to preserve milk until it is picked up by creamery trucks fall within the "agricultural producing" exemption.<sup>80</sup> In another case, a purchaser of water softeners had to pay no tax for softeners "used in industrial processing" which in this case meant renting them to stores, hotels, restaurants, and manufacturing plants. He was required to pay the levy for softeners rented to homeowners for domestic use.<sup>81</sup>

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crude oil through pipe lines from producing fields to a terminal. From there it was delivered to the refinery. Judicial discretion may have been in order here to distinguish between acquisition and production or processing.

<sup>74</sup> *Alabama Power Co. v. State*, *supra* note 63.

<sup>75</sup> 302 Mich. 643, 5 N.W.2d 516 (1942).

<sup>76</sup> *Id.* at 646, 5 N.W.2d at 517.

<sup>77</sup> Contrast this holding with the more restrictive approach of the Oklahoma court in *Southwest Chemical Supply, Inc. v. Oklahoma Tax Comm'n*, 352 P.2d 391 (Okla. 1960).

<sup>78</sup> *Supra* note 75, at 649-50, 5 N.W.2d at 518.

<sup>79</sup> *Ibid.*

<sup>80</sup> Mich. Pub. Acts, Act 167 § 1(b) (1933), as amended by Act 313 (1939).

<sup>81</sup> *Kress, d.b.a. Jackson Soft Water Service v. Dep't of Revenue*, 322 Mich. 590, 34

It cannot be overemphasized that the Michigan court never expressly referred to a theory of the sales taxation in any of these cases. In *Allied Dairy* it supported its approach by saying, "we have repeatedly held that the scope of the tax laws may not be extended by implication or a forced construction."<sup>82</sup> This argues against a too strict construction of the exemption, but the court cited no other principle of interpretation to justify its extreme liberalism. For this reason it may be concluded that the only reason for a difference between the Alabama and Michigan results is the phrase "industrial processing" as opposed to "processing, compounding, and manufacturing." Yet, the Michigan court certainly could have restricted "industrial processing" as Alabama restricted its provision. Perhaps the Michigan court simply did not express the economic theory that really guided its decisions. This in itself should be condemned. Nevertheless, these decisions of the Michigan Supreme Court can be justified as liberal construction of a broad "manufacturing" exemption designed to harmonize the sales tax with widely accepted notions of taxing only ultimate personal consumption. Unfortunately, the court never sought to uncover such a design.

### C. *Legislative Floundering*

The Wyoming Supreme Court employed the purposive approach in *State Board of Equalization v. Oil Wells Supply Co.*<sup>83</sup> Here again, the commissioner contended that an article could not be exempt unless it physically entered into the processed commodity. The court rightly rejected this contention, citing legislative history, the phrasing of the section at issue, and the "ultimate consumer" theory of sales taxation. The court found nothing very meaningful in the

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N.W.2d 501 (1948). The court required no tax on 10% of the softeners which the taxpayer established were used in "industrial processing." The court might have analyzed this case in terms of evasion and held taxpayer liable on all purchases of softeners. That is, when softeners may be so easily interchanged between "industrial" and domestic uses, the likelihood of evasion and the administrative difficulty of supervising are such that a legislative cross-purpose may arise to bring complete inclusion. See Professor Due's analysis note 35 *supra*.

<sup>82</sup> *Supra* note 75, at 650, 5 N.W.2d at 518.

<sup>83</sup> 51 Wyo. 226, 65 P.2d 1093 (1937). The relevant statute read:

Each purchase of tangible personal property or service made by a person engaged in the business of producing, furnishing, manufacturing, or compounding for sale, profit or use, any article, substance, service or commodity which is actually used in the production of, or enters into the processing of, or becomes an ingredient or component part of the article . . . he manufactures . . . shall be deemed a wholesale sale and shall be exempt from taxation under this act.

Wyo. C.L., C. 102 § 2(f) (1935).

statutory phrase "actually used in a production" and certainly cannot be criticized for this. The most that can be said for "actually" is that it was included to serve the same purpose as "directly" in other statutes.<sup>84</sup> Or, it may mean to differentiate between active use and idleness. But it hardly suggests, in context, that the "ingredients" rule alone must prevail.

The Wyoming legislature, however, was either unhappy with this interpretation or changed its mind, for in 1937 it enacted a new provision which excluded only "physical ingredients" and "furnished containers."<sup>85</sup> The extreme decision in another case<sup>86</sup> may have prompted this change, but if this were true the legislature could easily have amended so as to make clear that the court should distinguish between acquisition, administration, processing, and distribution. The lawmakers probably decided that the state needed more revenue than could be raised with a broad "used in manufacturing" exemption. Nevertheless, it seems clear that the court construed correctly in the *Wells Supply Co.* case while the legislature floundered in indecision about the extensiveness of the exemption.

Legislative ineptness accounted for a rather amusing interpretative difficulty in Michigan in the earliest days of the sales tax. The Michigan Legislature enacted Public Acts of 1933, Act No. 167, which proclaimed:

The term "sale at retail" means any transaction by which is transferred for consideration the ownership of tangible personal property, when such transfer is made in the ordinary course of the transferor's business and is made to the transferee for consumption or use or for any other purpose than for resale in the form of tangible personal property.

The Board of Tax Administration interpreted this provision to allow for an "ingredients" rule in the manufacturing area.<sup>87</sup> The legislature seemed dissatisfied, for on July 17, 1933, it passed the following resolution:

Resolved, that the legislative intent, in passing Act 167, Public Acts of 1933, was to exclude from provisions of the act any sale of any thing used exclusively in the manufacturing, assembling, producing, preparing, or wrapping, crating, and/or otherwise preparing for delivery any tangible personal property to be sold. . . .<sup>88</sup>

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<sup>84</sup> See text accompanying notes 90-95 *infra*.

<sup>85</sup> Wyo. C.L., C. 102 § 2(f) (1937).

<sup>86</sup> *Supra* note 73.

<sup>87</sup> All the background in this Michigan episode comes from the case of Boyer-Campbell Co. v. Fry, 271 Mich. 282, 260 N.W. 165 (1935).

<sup>88</sup> See note 87, *supra*.

Obviously, if this resolution meant for a broad "used in manufacturing" exemption to prevail in the state, the statutory "resale" language was hardly appropriate. Resolutions of this nature do not have the force of law.<sup>89</sup> Faced with this difficulty the administrators continued with the "ingredients" rule. One month later, the administrators decided to force the resolution into the statutory provision and declared a broad manufacturing exemption. However, on the advice of the State Attorney General, the administrative board returned to the "ingredients" rule. The legislature responded with another resolution requesting the board to comply with the prior resolution of intent. At this point, a number of manufacturers brought an action for declaratory judgment of their liability under the sales tax. The court, in an otherwise ambiguous decision, scolded: "The legislature attempted to clarify by resolution, when it should have expressed its intention clearly in the first instance or by later amendment."<sup>90</sup> The court could do little more than approve of the "physical ingredients" rule in this instance, for the "resale" language simply would not allow for broader construction unless "resale" were defined in the economic sense of cost being passed on to the ultimate consumer. The court can hardly be blamed for not countenancing this distortion. This decision evidently goaded the lawmakers into action, for in 1935 they amended the act to provide for the broad "used in industrial processing" exemption discussed earlier.

Some have tried to explain the peculiar legislative behavior in this episode.<sup>91</sup> Whatever the reason, the interpretative difficulty here stemmed from ineffective performance of the legislative rather than judicial function.

The best example of legislative floundering in the "manufacturing" area exists in statutes which exempt sales of property used or consumed "directly" in manufacturing, processing, etc..

A study of three states which operate with a statute of this nature reveals the difficulties involved. In Iowa, the word is nearly ignored. The Iowa Supreme Court has exempted waste removal equipment,<sup>92</sup> case packing machinery in a brewery,<sup>93</sup> and turbo-generators used by a manufacturer to produce electricity to run his plant.<sup>94</sup> The Iowa

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<sup>89</sup> 2 Sutherland, *Statutory Construction* 260-68, 3801-08 (3d ed. 1943).

<sup>90</sup> *Boyer-Campbell Co. v. Fry*, *supra* note 37, at 288, 260 N.W. at 171.

<sup>91</sup> Taylor, "Toward Rationality in a Retail Sales Tax," 5 *Nat'l Tax J.* 79 (1952).

<sup>92</sup> *City of Ames v. State Tax Comm'n*, 246 Iowa 1016, 71 N.W.2d 15 (1955). Compare *Alabama Power Co. v. State*, *supra* note 63.

<sup>93</sup> *Zoller Brewery Co. v. State Tax Comm'r*, 232 Iowa 1104, 5 N.W.2d 643 (1942).

<sup>94</sup> *Allis-Chalmers Mfg. Co. v. State Tax Comm'n*, 250 Iowa 193, 92 N.W.2d 129 (1958).

court announced its recognition of the word "directly,"<sup>95</sup> but the test seems to be whether the items involved provide for a more efficient manufacturing operation.<sup>96</sup>

In Georgia, on the other hand, the court saw nothing but the word "directly" in *State v. Cherokee Brick & Tile Co.*<sup>97</sup> A brick manufacturer had to pay a sales tax on artificial gas whose flame caused physical and chemical changes in raw materials used to produce the bricks. The court regarded "direct" as meaning no intervention of person or thing between the item and the manufactured product. Here, it was not the gas but the flaming gas and its heat that served as the catalyst. There was intervention of spark and combustion.

Ohio takes a middle ground between these extremes. The court interprets "directly" much as Alabama interprets its "used in manufacturing" exemption. The "chain of production" is key. The exemption seems to apply only to things,

absolutely necessary and most proximately used in the making of the product which is sold. Perhaps the test is better stated in the form of a question; namely: What is the minimum amount of equipment and materials necessary to make the product which is going to be sold?<sup>98</sup>

Perhaps "directly" should be construed as a directive to differentiate between manufacturing, acquisition, administration, etc., *i.e.*, that it is the legislature's way of assuring that "manufacturing" is limited in scope so that all sales to manufacturers are not exempted. Certainly, the lathe is more "directly" a part of producing goods than a typewriter or automobile. Yet, there is little basis for criticizing other views. The word "directly" is simply confusing and vague in this context. The word may indicate that the legislature is less concerned with pursuing theory than with raising revenue. Ohio, and conceivably even Georgia, may be best fulfilling the overriding legislative objective. Unless some rudiments of purpose can be gleaned from the circumstances surrounding the enactment, "directly" forces the court to rely heavily on intuitive powers in settling disputes.

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<sup>95</sup> *Dain Mfg. Co. v. Iowa State Tax Comm'n*, 237 Iowa 531, 22 N.W.2d 786 (1946).

<sup>96</sup> *City of Ames v. State Tax Comm'n*, *supra* note 92, at 1029, 71 N.W.2d at 23.

<sup>97</sup> 89 Ga. App. 235, 79 S.E.2d 322 (1953).

<sup>98</sup> Goffey, "Interpretation of Exemptions under the New Ohio Sales Tax," 30 U. Cinc. L. Rev. 457, 460 (1961). See, *e.g.*, *Anderson v. May*, 157 Ohio St. 407, 105 N.E.2d 648 (1952); *Jackson Iron & Steel Co. v. Glander*, 154 Ohio St. 369, 96 N.E.2d 21 (1950); *Mead Corporation v. Glander*, 153 Ohio St. 539, 93 N.E.2d 19 (1950); *Fyr-Fyter Co. v. Glander*, 150 Ohio St. 118, 80 N.E.2d 776 (1948); *Pioneer Linen Supply Co. v. Evatt*, 146 Ohio St. 248, 65 N.E.2d 711 (1946).



## III. SERVICES

Few states significantly tax services. Most limit the levy to sales of tangible personal property.<sup>99</sup> This has prompted courts to distinguish between transactions in which property is sold and those in which services are rendered with, perhaps, some property incidentally transferred. Much diversity of judicial opinion arises from this attempt. At least five different tests have evolved. Transactions may be of nontaxable services because:

(1) The materials used by the taxpayer in fulfilling his deal with his customer are destroyed in the process; they are not transferred as such to the customer.

(2) The final product could not be used generally by anyone other than the customer, either because a special order was involved which could be of no use to other buyers or because the article produced embodied the buyer's intangible property.

(3) The materials used constituted only an insignificant part of the cost of the job; the services provided by the taxpayer were the predominant factor in the charges made to the customer.

(4) The taxpayer's occupation is traditionally regarded by the community as the rendition of a service, not the sale of goods.<sup>100</sup>

Transactions may be taxable sales of property where the end-product transferred is tangible personal property so the tax should apply.

It has been suggested that courts err when they do not distinguish sales of property from services on the basis of the economic theories of consumption taxation.<sup>101</sup> Professor Hellerstein argues that courts should take cognizance of the fact that, with very few exceptions,<sup>102</sup> where a transaction is not taxed because it is regarded as the rendering of a service, the serviceman or repairer is considered the "consumer" of the articles employed in rendering the service. Thus, if the tax is not levied on the sale by the serviceman, it is levied on the sale by the supplier to the serviceman. The only real question then—"the stage at which the transaction is to be taxed."<sup>103</sup> If this is the issue, consumption taxation theories would lead courts to resolve doubts as to whether services or property are involved in a way to make the transaction one of "property." The tax would then be levied at the later stage.

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<sup>99</sup> Due, Sales Taxation 294-95 (1957).

<sup>100</sup> Hellerstein, "The Scope of the Taxable Sale Under Sales and Use Tax Acts: Sales as Distinguished from Services," 11 Tax L. Rev. 261, 272 (1956).

<sup>101</sup> *Id.* at 274.

<sup>102</sup> See text accompanying notes 117-36 *infra*.

<sup>103</sup> Hellerstein, *supra* note 101, at 273.

One must be sympathetic, however, with the judicial confusion in this area and hesitant to criticize. After all, there is no warrant in consumption tax theory for differentiating between expenditures for property and those for services. There are plausible legislative purposes that could have produced this distinction. One is a notion that there should be no "tax on labor,"<sup>104</sup> and another is the distaste for taxing such essential services as medical and dental care. Thus, purpose and theory assist little in answering the question of how to treat the optometrist or the printer. In the area of "manufacturing" provisions, there is room to chastise courts for a lack of appreciation of economic theory and the nonrestrictive interpretation implicit in it. In that area, the legislatures, at least with the "used in manufacturing" exemption, make an affirmative effort to comply with the fundamentals of "final personal consumption" theory. Here, however, the provision at issue allows for no impetus in the direction of expanding the word "property." There are legislative cross-purposes that cut directly against liberal construction. If anything, in this area, the legislature has manifested a purpose to subjugate economic theory to other more dominant considerations. At least this writer can sort out no dominant purpose for judicial guidance in distinguishing services from property. The difficulty, as with "directly" in the manufacturing area, seems inherent in the enactment. The court may have little alternative but to meander through dictionaries, trade practices, and other indicators of "ordinary" meanings. This, of course, does not excuse instances of obvious unfairness and discrimination in this area which are pointed out by Professor Hellerstein<sup>105</sup> and which certainly are not within the legislative purpose.

#### IV. SALES FOR RESALE

A definition of "retail sale" which includes sales for "use or consumption" and excludes "sales for resale" evidences a legislative attempt to avoid the evils of inequality of tax burden, pyramiding, and discrimination against non-integrated distribution systems of a turnover tax. With this in mind the courts should cooperate with the legislatures in construing statutes so as to circumvent these "evils." Yet some courts have not seen fit to do so, as a few cases dealing with containers demonstrate.<sup>106</sup> In these cases the transactions at issue were

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<sup>104</sup> Due, "Retail Sales Taxation in Theory and Practice," 3 Nat'l Tax J. 314, 320 (1950).

<sup>105</sup> Allowing repairmen and customers to determine tax liability by the statement of relative price charged for services and property seems quite irrational. See Hellerstein, *supra* note 100 at 282, 292.

<sup>106</sup> City Paper Co. v. Long, 235 Ala. 652, 180 So. 324 (1938); Wiseman v. Arkan-

sales of packaging material to retailers and manufacturers for use in distributing goods. The courts particularly focused on the fact that these retailers were not in the business of selling packaging goods to the public—only potatoes, biscuits, or shirts. This led to the conclusion that the containers involved were not sold for resale but for use by the retailer, and that it was immaterial that the cost to the retailer was passed on to the consumer.

But the fact that the cost is figured into the price of the resold item is not immaterial, since this gives rise to the "mischief" the legislature sought to mitigate. These courts could easily have construed "resale" to include this type of transaction by the retailer and certainly a definition of "use or consumption" in the sense of ultimate personal consumer could apply.<sup>107</sup> In a later Arkansas case<sup>108</sup> the court so construed "resale" when it was proved that the packaging added twelve to fourteen cents to the price of the goods involved. The court evidently needed a vivid picture of the economic realities.

There may be some reason, however, for taxing containers sold to the merchant or manufacturer, although the courts never mention it. If a state taxes all producer goods and exempts only "sales for resale" it seems clear that the legislature is not particularly concerned about production integration, pyramiding, or inequitable tax burdens. It is primarily seeking to remedy vertical distribution integration. The taxation of containers may bring about the former "evils," but not the latter. Thus, the legislative purpose behind the "resale" phraseology does not necessarily extend to packaging material. All states do at least have a "physical ingredients" rule and this indicates concern for "evils" other than the merging of the distribution system. But unless the state's legislature has enacted a fairly broad manufacturing exemption, the court may be justified in finding no directive to categorize container transactions as "sales for resale" rather than for "use or consumption."

As seen earlier, Alabama does broadly exempt producer goods. It is instructive to follow the fate of containers in that state. In 1939, the legislature added to the "physical ingredients" portion of its "wholesale sale" definition so that it exempted the "furnished containers" of a "manufactured or compounded" product.<sup>109</sup> Why did it

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sas Wholesale Grocers Ass'n, 192 Ark. 313, 90 S.W.2d 981 (1937); *Warren v. Fink*, 146 Kan. 716, 97 N.W.2d 384 (1937).

<sup>107</sup> For this approach, see, e.g., *American Molasses Co. v. McGoldrick*, 281 N.Y. 269, 22 N.E.2d 369 (1939).

<sup>108</sup> *McCarroll v. Scott Paper Box Co.*, 195 Ark. 1105, 93 S.W.2d 453 (1938).

<sup>109</sup> Ala. Code, tit. 51, § 752 (1958):

The term "wholesale sale" shall include a sale of tangible personal property

limit the change to containers of "manufactured or compounded" products? Was this a directive to the court to continue construing as retail sales transfers of material that packaged unaltered goods sold by a retailer? This question faced the Alabama court in *State v. Albright & Wood, Inc.*<sup>110</sup> The court answered in the affirmative on the ground that a case decided just before the legislative change apparently allowed taxation of bottles and boxes which packaged both compounded and unaltered goods. The change was responsive to only the former levy—the implication being that the legislature approved the levy on the latter containers.<sup>111</sup>

It is not possible to strongly criticize this decision, but it can be questioned. Arguably that the more accurate implication was that the legislature wanted to exempt all containers. In other words, the 1939 enactment can be seen as giving momentum to the inclusion of container sales in the term "sales for resale" rather than drawing the outer limits of container exemption. Comparing the 1939 act with its predecessor,<sup>112</sup> the word "compounded" had no special significance. It appeared in the earlier act so that it cannot be said to exist only as a partial reaction to the container decisions. A reasonable way to read the series of enactments is simply to say that the "furnished container" provision was a reaction to the container decisions; it was tacked on to the "physical ingredients" provision because this seemed most convenient; and the fact that the "ingredients" provision contained the word "compounded" should not significantly influence interpretation of the "resale" provision. The only significant fact is that the legislature saw taxation of furnished containers as impeding its overall effort to tax final personal consumption. This is particularly true in light of Alabama's broad "machines in manufacturing" exemption.<sup>113</sup>

By far the most interesting skirmish in the "resale" area took place in Illinois. The Illinois statute,<sup>114</sup> passed in 1933, could not be

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or products (including iron ore) to a manufacturer or compounder which enters into and becomes an ingredient or component part of the tangible personal property or products which he manufactures or compounds for sale, and the furnished container and label thereof.

<sup>110</sup> 268 Ala. 607, 109 So. 2d 844 (1959).

<sup>111</sup> *Durr Drug Co. v. Long*, 237 Ala. 689, 188 So. 873 (1939).

<sup>112</sup> The term "wholesale sale" shall include a sale of tangible personal property or products to a manufacturer, mine, quarry operator, or compounder which enters into and becomes an ingredient or component part of the tangible personal property or products which he manufactures and machinery used in such compounding, mining, quarry operator [sic], manufacturing, or processing.

Ala. G.A. Act 126, p. 126 (1936-37).

<sup>113</sup> Ala. Code tit. 51, § 755(p) (1940).

<sup>114</sup> "Sale at retail" means any transfer of the ownership of, or title to, tangible

labeled sales tax since that was prohibited by the state constitution, so it was imposed on the privilege of selling at retail.

The first pertinent case under the statute was *Bradley Supply Co. v. Ames*,<sup>115</sup> which held that those engaged in the occupation of selling plumbing supplies to contractors were not subject to tax. The contractors were not the ultimate "users or consumers" since they transferred the supplies to the owner of the real estate. Here was a neat application of "final consumer" economics.

The difficulty began when the question of tax liability of the contractors arose. In *Herlihy Mid-Continent Co. v. Nudelman*,<sup>116</sup> the court held that, "plaintiffs did not hold themselves out as vendors of the materials finished. . . ."<sup>117</sup> The identity of the materials was destroyed, and if there was any sale, it was of the completed sewers ready to be used. So, there could be no occupation tax on the contractors since they did not sell tangible personal property. Thus there was no tax anywhere along the line. This anomaly spread throughout the services area. Shoe repairmen,<sup>118</sup> optometrists<sup>119</sup> and doctors<sup>120</sup> paid no tax because they did not vend but only transferred property incidentally with the furnishing of services. On the other hand, vendors of leather to shoe repairmen,<sup>121</sup> of optical goods to optometrists,<sup>122</sup> and of medical supplies to hospitals and doctors<sup>123</sup> suffered no levy since they did not sell to the ultimate "users or consumers."

At this point, was the court in error? It would seem that the court should have abandoned the consumption taxation meaning or, as the Illinois court put it, "the ordinary and popular meaning"<sup>124</sup> of the words "use or consumption." It was wise to read this meaning in at the outset, perhaps, as a manifestation of legislative purpose but not when it became clear that no tax at all would be paid. The discrimination in favor of service industries (or, if there was little shifting, the suppliers who happened to sell to them) was immense, as was the loss of revenue. But something can be said for the judicial position.

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personal property to the purchaser for use or consumption and not for resale in any form as tangible personal property, for a valuable consideration.

Ill. Ann. Stat. ch. 120, § 440 (Smith-Hurd 1954).

<sup>115</sup> 359 Ill. 162, 194 N.E. 272 (1934).

<sup>116</sup> 357 Ill. 600, 12 N.E.2d 638 (1938).

<sup>117</sup> *Id.* at 604-05, 640.

<sup>118</sup> *Revzan v. Nudelman*, 370 Ill. 180, 18 N.E.2d 218 (1939).

<sup>119</sup> *Babcock v. Nudelman*, 367 Ill. 626, 12 N.E.2d 635 (1938).

<sup>120</sup> *Huston Brothers v. McKibbin*, 386 Ill. 479, 54 N.E.2d 564 (1944).

<sup>121</sup> *Revzan v. Nudelman*, *supra* note 118.

<sup>122</sup> *American Optical Co. v. Nudelman*, 370 Ill. 627, 19 N.E.2d 582 (1939).

<sup>123</sup> *Miller Co. v. Department of Finance*, 372 Ill. 598, 25 N.E.2d 43 (1939).

<sup>124</sup> *Bradley Supply Co. v. Ames*, *supra* note 115, at 166, 194 N.E. at 276.

The legislature obviously had in mind discrimination against non-service industries when it enacted the statute and it is not a likely legislative objective to have taxation of a vendor depend on whether the vendee will be taxed or exempted as a serviceman.

This support for the judicial position disappeared, however, in 1941 when the legislature amended the act as follows:

"Use or consumption," in addition to its usual and popular meaning, shall be construed to include the employment of tangible personal property by persons engaged in service occupations . . . , where as a necessary incident to the rendering of such services, transfer of all or a part of the tangible personal property employed in connection with the rendering of said services is made from the person engaged in the service occupation . . . , to his customer or client.<sup>125</sup>

Where the legislature so clearly expressed itself as desirous of having a tax paid on the transfer of goods to the serviceman and even provided for the word construction that would allow it to happen, a court must have irrefutable reasons for adhering to another construction even if the other construction is soundly based on economic theory or common experience. Nevertheless, the Illinois court stayed with its original interpretation of "use or consumption."

The *Stolzer Lumber*<sup>126</sup> case involved a lumber dealer who sold to contractors. The court found the amendment invalid and the materialmen not liable because the amendment was inconsistent with the title of the act. It said:

The transfer of property from the contractor to the owner contemplated in the amendment, is clearly a transfer in some form for a valuable consideration . . . . It is clearly apparent therefore that this amendment introduces an inconsistency in the Retailers' Occupation Tax Act and evidences an intent to call that a retail sale which not only the statute itself declares shall not be such, but which cannot, in view of the purpose of the act and settled meaning of the term, be so defined. . . . Both the title and the provisions of the act relate to a tax upon persons engaged in the business of selling tangible personal property "to purchasers for use or consumption." "To purchasers for use or consumption," must, both by commonly understood meaning and by the construction which this court has given to the language of the act and its title, be construed to mean, for use or consumption by such ultimate purchasers. Such language must also mean a sale where the article sold is not to be, in any form, transferred or resold for a valuable consideration, since such a sale would not be for the use or consumption of such purchaser, as the title and the act provide.<sup>127</sup>

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<sup>125</sup> Ill. Ann. Stat. ch. 120, § 440 (Smith-Hurd 1954).

<sup>126</sup> 386 Ill. 334, 54 N.E.2d 554 (1944).

<sup>127</sup> *Id.* at 340, 54 N.E.2d at 557.

The cited paragraph presents precisely the kind of judicial logic which should be eschewed. It builds a fortress out of "commonly understood meaning" and previous judicial construction. The court speaks of legislative purpose but suppresses an express statement which manifests a supervening cross-purpose to levy a tax on suppliers of servicemen so that some revenue is raised in the chain of transactions. It is not a "fact" that the "user or consumer" of the title must be the ultimate "user or consumer." These words have no factual meaning apart from compliance with legislative purpose. If the word "consumer" cannot bear the meaning best suited to fulfilling the expressed legislative cross-purpose,<sup>128</sup> certainly the word "user" will ably serve. It can mean ultimate "user" in one fact situation and temporary "user" in another. Furthermore, the phrase "not for resale as tangible personal property" can be narrowed to exclude sales where property is resold only incidentally to the rendering of services if this complies with the clear legislative objective.<sup>129</sup>

A court might be justified in hesitating to engage in this definitional hair-splitting as an original proposition, but to refuse to do so in the face of a legislative mandate is judicial enactment rather than judicial interpretation.

Eight years later, the Illinois court showed signs of enlightened interpretation in *Modern Dairy v. Dep't of Revenue*.<sup>130</sup> In this case, the taxpayer dairy sold milk to a state hospital which gave the milk free to its patients. The court defined "use" as "any employment of a thing which took it off the retail market so that it was no longer the object of a tax on the privilege of selling it at retail."<sup>131</sup>

But this bright light was snuffed out the next year in *Burrows v. Hollingsworth*.<sup>132</sup> The taxpayer pharmaceutical companies sold medicines and other medical supplies to doctors and hospitals, previously declared servicemen. The court stressed that,

a person is not engaged in the business of selling at retail unless he transfers tangible personal property (1) for use or consumption and (2) not for resale in any form as tangible personal property. Both tests must be met to justify the imposition of the tax.<sup>133</sup>

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<sup>128</sup> However, the serviceman was considered the ultimate consumer in *Mendoza Fur Dying Works, Inc. v. Taylor*, 272 N.Y. 275, 5 N.E.2d 818 (1936); *W. J. Sandberg Co. v. State Bd. of Assessment & Review*, 225 Iowa 103, 278 N.W. 643 (1938).

<sup>129</sup> Hart & Sacks, *The Legal Process; Basic Problems in the Making and Application of Law* 89-102 (tent. ed. 1958).

<sup>130</sup> 413 Ill. 53, 108 N.E.2d 8 (1952).

<sup>131</sup> *Id.* at 15, 108 N.E.2d at 67.

<sup>132</sup> 415 Ill. 202, 113 N.E.2d 169 (1953).

<sup>133</sup> *Id.* at 174, 113 N.E.2d at 208.

The court accepted the *Modern Dairy* definition of "use" but distinguished that case on the ground that in it there was no resale to the patients for valuable consideration as in the instant case. Thus, unlike *Modern Dairy*, this case did not meet the second requirement.

And this is the way the judiciary left the interpretative problem before it. Indeed, the court in *G. S. Lyon & Sons Lumber & Mfg. Co. v. Dep't of Revenue*<sup>134</sup> taxed sales by materialmen to builders and overturned the whole line of construction cases. But the court, although using broad language, still concerned itself with the second requirement and said it was met since the resale by the builder was of real property and not tangible personal property. Thus, "the sale to the builder is the last transfer of the materials as personal property, and is a sale for use or consumption within the meaning of the act."<sup>135</sup> The court only cleverly skirted the second requirement instead of meeting it directly and construing "resale" to coincide with announced legislative purpose. The legislature mooted much of this judicial discussion by enacting the Service Occupation Tax, effective August, 1961.<sup>136</sup> It taxes servicemen on the cost price of tangible personal property which they purchase from suppliers and retransfer as an incident to rendering of services.

#### CONCLUSION

Statutory interpretation requires exhaustive intellectual effort. A proper approach does not necessarily ease the difficulty: it helps to make the results rationally sound. Some courts have not employed the purposive approach. The Michigan and Alabama Supreme Courts are examples. They drifted aimlessly through dictionaries searching for the most oft-repeated meaning, or they spoke of "fair" construction. This cannot be rationally defended even though purpose, at times, supported the result. Other courts did refer to purpose, but the results usually were disappointing. At times elaborate statements about purpose were like a ritual which was prerequisite to entering the realm of statutory interpretation. On gaining entrance, the statements were forgotten. At other times the result reflected faulty reasoning; or, the courts simply demonstrated a lack of hard work—too much willingness to be guided by a superficial "purpose" instead of pursuing the more basic and controlling.

But the courts in the sales tax area face extraordinary obstacles to

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<sup>134</sup> 23 Ill. 2d 180, 177 N.E.2d 316 (1961). See also *Material Service Corp. v. Dep't of Revenue*, 25 Ill. 2d 137, 183 N.E.2d 164 (1962).

<sup>135</sup> 23 Ill. 2d at 184, 177 N.E.2d at 319.

<sup>136</sup> Ill. Ann. Stat. ch. 120, §§ 103-06 (Smith-Hurd Supp. 1965).



applying (intelligently) the purposive approach. The legislators enact amorphous statutes which are so fraught with cross-purposes that the approach often lends little assistance. Also, a proper resolution of cases in the area often requires some awareness of economic theory.

The courts can do little about the first obstacle except strive to be equitable and consistent. The second obstacle raises interesting questions about the process of litigation. Should courts be held responsible for the intricacies of the economic theory of sales taxation? Where reasoned elaboration of the legislative directive is impossible without knowledge of the economic theory which it advances or rejects, the economic theory must be explored. The goal must be rationality, and rationality requires knowledge.

How can the court acquire the necessary knowledge? Administrators could assist somewhat, but reasonable doubts arise concerning their sophistication in economics. The regulations could contain more intensive background analysis. Faced with the task of more fully expressing the reasons in support, administrators might frame rules more soundly based on legislative purpose. But, probably the primary source of information must be the lawyer's brief. As in anti-trust cases, sales tax litigation calls for versatile lawyering—lawyers with great facility for blending economic and legal concepts. Lawyers must fully appreciate and develop legislative purpose before the judiciary can be made to shoulder blame for faulty decision making where purpose is ascertainable.

The problems are complex. The legislator, the judge, and the lawyer have much work to do. Until each fully meets institutional and professional responsibilities, the proper rationality cannot determine the solutions.