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IN THE COURT OF APPEALS OF TENNESSEE
AT NASHVILLE
March 8, 2023 Session

ALSCO, INC. v. TENNESSEE DEPARTMENT OF REVENUE

Appeal from the Chancery Court for Davidson County
No. 21-1055-III Ellen Hobbs Lyle, Chancellor

No. M2022-01019-COA-R3-CV

CARMA DENNIS MCGEE, J., dissenting.

I respectfully dissent from the majority opinion. As the majority notes, an administrative judge determined that the taxpayer's sanitizing operations in this case do not constitute "manufacturing" as they are not "processing" tangible personal property. The administrative judge reasoned that a taxpayer is required to show that its activity fundamentally changes or transforms the property from the state or form in which it originally existed. Applying that standard, the administrative judge found that the state or form of the linens has not been changed or altered by the cleaning, as they remain the same linens before and after.

The majority correctly sets out the standard of review of the administrative judge's decision and notes that tax exemption statutes are to be strictly construed against the taxpayer. However, respectfully, I cannot agree with their application of the same in this matter and the conclusion at which they have arrived. "'[C]onstruction of a statute and application of the law to the facts is a question of law that may be addressed by the courts.'" *All Access Coach Leasing, LLC v. McCord*, No. M2020-01368-COA-R3-CV, 2021 WL 4999300, at *7 (Tenn. Ct. App. Oct. 28, 2021) (quoting *Concord Enterprises of Knoxville, Inc. v. Comm'r of Tenn. Dep't of Lab. & Workforce Dev.*, 524 S.W.3d 233, 236 (Tenn. Ct. App. 2017)). "Still, we have emphasized in the UAPA context that '[t]he courts may [not] substitute their judgment for the [agency's], even if the evidence could support a conclusion different from the one reached by the commission.'" *Id.* (quoting *Miller v. Civ. Serv. Comm'n of Metro. Gov't of Nashville & Davidson Cty.*, 271 S.W.3d 659, 664 (Tenn. Ct. App. 2008)). "[A]gencies are entitled to deference in their interpretations of rules, regulations, and statutes that they are charged with administering." *Id.* at *8. In addition, as the majority notes, tax exemption statutes are construed against the taxpayer, and any well-founded doubt is sufficient to defeat a claimed exemption. *Nashville Clubhouse Inn v. Johnson*, 27 S.W.3d 542, 544 (Tenn. Ct. App. 2000).

Bearing these principles in mind, I would defer to the decision of the administrative judge. According to the Tennessee Supreme Court, "processing" is "'essentially a transformation or conversion of materials or things into a different state or form from that in which they originally existed—the actual operation incident to changing them into marketable products.'" *Beare Co. v. Tenn. Dep't of Revenue*, 858 S.W.2d 906, 908 (Tenn. 1993) (quoting *Gressel Produce Co. v. Kosydar*, 297 N.E.2d 532, 535 (Ohio 1973)).[1] Our Supreme Court quoted this definition from the *Gressel* case involving raw eggs. There, the taxpayers had acquired eggs from farms, placed them in coolers, then put them through a washer that utilized "an aqueous solution of soap, water softener, salt, chlorine and defoamer," followed by a coating of mineral oil and packaging. 297 N.E.2d at 533. Still, the *Gressel* Court held that this operation resulted in "no change in the state or form of the eggs, regardless of the fact that they may have been enhanced in value." *Id.* at 536.

As the majority notes, in a later case, the Ohio Supreme Court concluded that "laundry companies change the state of the articles laundered" because "[t]hey physically remove dirt, grime, oil, and other contaminants from the fibers, changing the state of the article to a clean product." *Van Dyne Crotty Co. v. Limbach*, 53 Ohio St. 3d 3, 3 (1990).[2] More recently, however, the Tennessee Court of Appeals applied the same definition of "processing" from *Gressel* and *Beare* to a dry-cleaning and laundering business, in the reported case of *Walker's, Inc. v. Farr*, 338 S.W.3d 887, 893-95 (Tenn. Ct. App. 2010), to determine whether "processing" had occurred. We noted that "processing" was defined by the Court as "'[E]ssentially a transformation or conversion of materials or things into a different state or form from that in which they originally existed [--] the actual operation incident to changing them into marketable products.'" *Id.* (quoting *Beare*, 858 S.W.2d at 908). Considering the facts before us in light of this definition, we found "nothing in the appellate record indicating that the laundering and dry-cleaning services sold by Walker's resulted in a change in state or form." Instead, we found the dry-cleaning and laundering service to be "more akin to" the egg case, which involved cleaning and application of oil to eggs but "did not constitute 'processing'" of them. *Id.* Simply put, the laundering and dry-cleaning may have resulted in a clean product, but this did not result in "a change in state or form."

Although the majority is persuaded by and relies on the reasoning of the Ohio Supreme Court in *Van Dyne*, I feel that they have ignored controlling precedent from our

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[1] The majority notes that the sales and use tax statutes do not define the term "processing," but they do contain a definition of the phrase "Fabricating or processing tangible personal property for resale." Tenn. Code Ann. § 67-6-102(39). It is not particularly helpful here, but the definition does provide that "'Fabricating or processing tangible personal property for resale' shall be deemed to include providing fabrication and repair services to aircraft" but "shall not include any other type of repair services." *Id.*

[2] The Court distinguished "the cleaning activity in *Gressel*" by stating that "the laundry companies here do not simply enhance the marketability of their product; they actually change, in these operations, the articles into marketable products." *Van Dyne*, 558 N.E.2d at 48.

own Court. I cannot distinguish this case from that case, although they take great pains to do so. There is no real difference between the taxpayer's sanitizing process and dry cleaning, or even laundering. In the end it is just cleaning. Moreover, soiled linen or dirty fabric is just that, regardless of whether that fabric is part of a dress, pants, uniforms, bar towels, etc.

Ultimately, the majority concludes that the taxpayer's sanitization operation results in textiles undergoing "a change in state or form" – from soiled to sanitized. Thus, the majority concludes that the textiles have undergone a change in state. Considering our standard of review on appeal, the principles applicable to tax exemption statutes, this Court's decision in *Walker's* regarding dry-cleaning and laundering services, and a common sense interpretation of the terms at issue, I must respectfully dissent. As the administrative judge found, "[t]he state or form of the linens in no way [has] been altered—they are the same uniforms, bar towels, etc. both before and after cleaning."

CARMA DENNIS MCGEE, JUDGE