JONES DAY

COMMENTARY

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IN SHORT

The Decision: In *Waste Management of Illinois, Inc. v. Illinois Department of Revenue*, 2017 IL App (1st) 162830-U, the Illinois Appellate Court held that compressed natural gas ("CNG") is not a taxable motor fuel under the Illinois Motor Fuel Tax Law.

The Result: This is the first appellate decision to overturn the Illinois Independent Tax Tribunal ("Tax Tribunal").

Looking Ahead: For all periods *prior to* June 30, 2017, taxpayers should be able to cite the *Waste Management* order as the factual basis for a refund claim. For periods *after* that date, taxpayers can challenge Public Act 100-0009 if they are willing to pay up-front the tax under protest, and litigate the issue in a circuit court.

Waste Management of Illinois, Inc. ("Waste Management") filed suit in the Tax Tribunal contesting denial by the Illinois Department of Revenue ("Department") of its claims for refund of motor fuel tax paid on its use of CNG in its fleet. The Department adopted a regulation in 2014 that implied that CNG was subject to Illinois motor fuel tax. Waste Management argued that the statute defines "Motor Fuel" as a liquid, and since CNG is not a liquid, CNG is not taxable. Waste Management further contended that the Department's regulations purporting to levy a tax on CNG were an unconstitutional act of legislation by an Executive agency.

On cross-motions for summary judgment, the Tax Tribunal ruled in the Department's favor, stating that the overall purpose of the statute was to tax all fuels, thus overriding the fact that the definition of "taxable motor fuel" is limited to liquid fuels. Waste Management appealed to the Illinois Appellate Court. Before the court ruled, but after the case was fully briefed, the General Assembly amended the Motor Fuel Tax Law on June 30, 2017, without changing the definition of "Motor Fuel" at issue in the appeal, to provide that "*Beginning January 1, 1990*, the rate of tax imposed in this paragraph, *including the tax on compressed natural gas*, shall be 19 cents per gallon" (emphasis added; amending language underlined).

> Notwithstanding the drafters' sleight of hand, Public Act 100-0009 did not amend the definition of 'Motor Fuel,' so the definition is *still* limited to liquid fuels.

On December 29, 2017, the appellate court ruled in favor of Waste Management. The court wrote, "[a] plain reading of the statutory definition of 'Motor Fuel' shows that the legislature did not intend to include combustible gases such as CNG … as a product subject to a tax under the Act." Since CNG is not a liquid, it cannot be a taxable motor fuel when the definition of such fuels is limited to liquid fuels. Ruling on purely statutory grounds, the court did not address Waste Management's arguments about the invalidity of the Department's regulations. Regarding Public Act 100-0009, the appellate court said the amendment was "prospective in nature," so it would not consider the legislative changes in rendering its decision on prior periods at issue in the case. Although the court overturned the Tax Tribunal, it issued its decision as a "Rule 23" order instead of a published opinion, which means it cannot be cited as precedent by other litigants.

The state filed a petition for rehearing, which the appellate court denied, and the state declined to petition the Illinois Supreme Court for review, so the court's decision is final.

The changes in P.A. 100-0009 give the illusion that compressed natural gas has been a taxable motor fuel since January 1, 1990. Notwithstanding the drafters' sleight of hand, P.A. 100-0009 did not amend the definition of "Motor Fuel," so the definition is *still* limited to liquid fuels. Further, the court noted, "the General Assembly did not include any express statement regarding the temporal reach of the amendments to the Act" and therefore ruled that the changes made by P.A. 100-0009 were prospective only. Indeed, a legislative change *retroactive for* a 27-year period would surely raise constitutional concerns.

The murky retroactivity in P.A. 100-0009 and the issuance of a Rule 23 order instead of a precedential opinion in *Waste Management* leave taxpayers with unfair procedural choices. The scientific facts about CNG in the appellate record were stipulated by the Department, so for all periods *prior to* June 30, 2017, taxpayers should be able to cite the *Waste Management* order as the factual basis for a refund claim.

However, if the Department insists on denying the claims for lack of a precedential opinion, taxpayers must then protest the denials in the Tax Tribunal. Any taxpayers wishing to litigate the constitutionality of P.A. 100-009 if it is asserted to retroactively bar the claim will face a frustrating obstacle. The Tax Tribunal cannot rule on the validity of statutes—it can only prepare a record on the issue for the appellate court to address constitutional issues *de novo* on appeal.

For periods *after* June 30, 2017, taxpayers can challenge P.A. 100-009 and its failure to amend the definitions through the use of the "Protest Monies Act" if they are willing to pay up front the tax on CNG under protest, and litigate the issue in a circuit court that has the authority to declare laws invalid.

Jones Day represented Waste Management in this case.

THREE KEY TAKEAWAYS

1. The Illinois Appellate Court's nonprecedential order that CNG is not a taxable motor fuel, and subsequent legislation, make the treatment for other taxpayers less certain.
2. Taxpayers may bring refund claims for Illinois motor fuel tax paid on CNG.
3. The options for disputing any denial of a refund claim, a current liability, or a future audit assessment of tax depend on the tax periods involved and the particular facts of the taxpayer.

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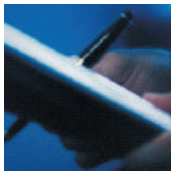
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