

## IL Appellate Court – compressed natural gas not subject to motor fuel tax

### Overview

In a unanimous, unpublished order issued on December 29, 2017, the Illinois First District Appellate Court (“Appellate Court”) reversed an earlier Illinois Independent Tax Tribunal (“Tax Tribunal”) order which had granted summary judgment in favor of the Illinois Department of Revenue (“Department”).<sup>1</sup> Ruling in favor of the taxpayer, the Appellate Court held that compressed natural gas (“CNG”) is not a taxable motor fuel under the Illinois Motor Fuel Tax Law Act (“Motor Fuel Tax”).<sup>2</sup> The Appellate Court’s order is subject to discretionary review by the Illinois Supreme Court upon the Illinois Department of Revenue filing an appeal.

This tax alert summarizes the factual background of the case, the Tax Tribunal’s and Appellate Court’s decisions, and provides taxpayer refund considerations.

### Background

Illinois imposes a per gallon excise tax on “all motor fuel used in motor vehicles operating on [Illinois] public highways.”<sup>3</sup> For purposes of the Motor Fuel Tax Law Act, “motor fuel” is defined as:

[A]ll volatile and inflammable *liquids* produced, blended or compounded for the purpose of, or which are suitable or practicable for, operating motor vehicles. Among other things, “Motor Fuel” includes “*Special Fuel*” as defined in Section 1.13 of this Act.<sup>4</sup>

“Special fuel,” in turn, is defined as:

[A]ll volatile and inflammable *liquids* capable of being used for the generation of power in an internal combustion engine except that it does not include gasoline as defined in Section 5, example (A), of this Act, or combustible gases as defined in Section 5, example (B), of this Act . . .<sup>5</sup>

The taxpayer’s fleet included CNG-fueled motor vehicles that provided waste collection, transfer, recycling, and disposal services in Illinois.<sup>6</sup> In order to fuel its CNG fleet, the taxpayer produced its own CNG by purchasing pipeline natural gas from a natural gas supplier and compressing the natural gas into CNG. The taxpayer then dispensed the CNG into his own CNG-powered motor vehicles.<sup>7</sup> Natural gas does not become a liquid at any point in the production process nor upon consumption in a motor vehicle.<sup>8</sup>

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<sup>1</sup> *Waste Management of Illinois, Inc. v. The Illinois Independent Tax Tribunal*, No. 1-16-2830 (1<sup>st</sup> Dist., Dec. 29, 2017) (unpublished order under Supreme Court Rule 23). A copy of the First District Appellate Court’s order is available [here](#).

<sup>2</sup> *Id.*

<sup>3</sup> 35 ILL. COMP. STAT. ANN. 505/2(a).

<sup>4</sup> 35 ILL. COMP. STAT. ANN. 505/1.1 (emphasis added).

<sup>5</sup> 35 ILL. COMP. STAT. ANN. 505/1.13 (emphasis added).

<sup>6</sup> *Waste Management of Illinois, Inc.*, No. 1-16-2830 at ¶ 4.

<sup>7</sup> *Id.*

<sup>8</sup> *Id.* at ¶ 5.

### Tax Tribunal summary judgement order

During the period at issue, the taxpayer paid the Motor Fuel Tax and subsequently filed refund claims seeking to recover the disputed overpayment of Motor Fuel Tax paid on the CNG, contending that the statutory definitions unambiguously defined "Motor Fuel" as a liquid, and that CNG is not a liquid.<sup>9</sup> The Department denied the taxpayer's refund requests and determined that CNG was a taxable fuel under the statutory definition of motor fuel.<sup>10</sup>

Taxpayer filed a petition for review with the Tax Tribunal asserting that CNG is not a taxable "Motor Fuel" under the Motor Fuel Tax laws.<sup>11</sup> On October 3, 2016, the Tax Tribunal issued a written order granting summary judgment in favor of the Department and concluded that CNG was a taxable "Motor Fuel."<sup>12</sup>

### Appellate Court order

Reversing the order of the Tax Tribunal, the Appellate Court determined that the definition of Motor Fuel "is unambiguous and does not include CNG" in the statutory definition.<sup>13</sup> The Appellate Court looked to the plain language of the statute and noted that the first sentence of the definition specifically refers to and includes only liquids.<sup>14</sup> The second sentence in the definition states that "Motor Fuel" includes "Special Fuel," separately defined as "all volatile and inflammable liquids capable of being used for the generation of power in an internal combustion engine except that it does not include . . . combustible gases . . ." <sup>15</sup> Therefore, the Appellate Court determined that the legislature did not intend to include "combustible gases", such as CNG, in the definitions of "Motor Fuel" and "Special Fuel" subject to Motor Fuel Tax.<sup>16</sup>

Furthermore, the Appellate Court rejected the Department's argument that the phrase "among other things" in the definition of "Motor Fuel" casts a sufficiently encompassing reference to tax CNG as a "Motor Fuel".<sup>17</sup> The Appellate Court stated that accepting the Department's argument would produce an "absurd" result—a nonliquid combustible gas such as CNG being subject to the Motor Fuel Tax because it falls within the category of "among other things," while at the same time CNG is specifically excluded from the Motor Fuel Tax definition of "Special Fuel" and "Motor Fuel" as a "combustible gas."<sup>18</sup> The Court stated that if the legislature had intended for combustible gases to be subject to Motor Fuel Tax, the legislature would have included combustible gases in the definition of "Motor Fuel."<sup>19</sup> Accordingly, the Appellate Court ultimately held that CNG does not fall within the definition of "Motor Fuel" and is not subject to the Motor Fuel Tax.<sup>20</sup>

### Considerations

If the Department seeks leave to appeal, the Appellate Court decision is subject to discretionary review by the Illinois Supreme Court. During the interim, taxpayers that paid the Motor Fuel Tax on CNG used in their fleet of vehicles should consult with their tax advisors relative to filing Illinois Motor Fuel Tax refund claims based on the logic of the decision.<sup>21</sup>

## Contacts:

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<sup>9</sup> *Id.* at ¶ 7.

<sup>10</sup> *Id.* at ¶ 6.

<sup>11</sup> *Id.* at ¶ 7.

<sup>12</sup> *Waste Management of Illinois, Inc. v. Illinois Department of Revenue*, 15 TT 130 (Oct. 3, 2016).

<sup>13</sup> *Waste Management of Illinois, Inc.*, No. 1-16-2830 at ¶ 19.

<sup>14</sup> *Id.*

<sup>15</sup> 35 ILL. COMP. STAT. ANN. 505/1.13.

<sup>16</sup> *Waste Management of Illinois, Inc.*, No. 1-16-2830 at ¶ 20.

<sup>17</sup> *Id.* at ¶ 22.

<sup>18</sup> *Id.*

<sup>19</sup> *Id.*

<sup>20</sup> *Id.* at ¶ 26.

<sup>21</sup> The statute of limitations for filing Motor Fuel Tax refund claims is two years from the date tax was paid by the refund claimant. 35 ILL. COMP. STAT. ANN. 505/13.

## External Multistate Tax Alert

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