

Tax Trends

The newsletter of the Illinois State Bar Association's Section on State & Local Taxation

Illinois Appellate Court Holds Lowe's Violated the Illinois False Claims Act by Remitting Illinois Use Tax and Not Retailers' Occupation Tax on Certain Appliance Sales After Receiving Guidance in 2015 Department of Revenue Compliance Alert

Illinois Appellate Court Holds Lowe's Violated the Illinois False Claims Act by Remitting Illinois Use Tax and Not Retailers' Occupation Tax on Certain Appliance Sales After Receiving Guidance in 2015 Department of Revenue Compliance Alert

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ON SEPTEMBER 30, 2024, THE ILLINOIS Appellate Court issued an Order in *People of the State of Illinois, ex rel., Richard Lindblom and Ralph Lindblom v. Lowe's Home Centers, LLC, Sears Brands, LLC, Home Depot U.S.A., Inc., Best Buy Stores, L.P., and Gregg Appliances, Inc.*, 2024 IL App (1st) 231163-U, Second Division (September 30, 2024), affirming in part and reversing in part the trial court's judgment finding Lowe's Home Centers, LLC (hereafter "Lowe's") liable for violating the Illinois False Claims Act and remanding matter for a new trial on the issue of damages.

By way of background, the Lindbloms own and operate a retail appliance store in Schaumburg, Illinois. The Lindblom's store is a direct competitor of Lowe's. The Lindbloms sell appliances, including dishwashers and microwaves, at their Schaumburg store and charge their customers the Illinois Retailers' Occupation Tax (hereafter "ROT" or "sales tax"). Lowe's also sells similar appliances but did not charge its customers the Illinois sales tax (but did pay Illinois use tax on the cost price of the appliances). In February of 2015, the Lindbloms contacted the Illinois Department of Revenue (hereafter "Department") and alleged that Lowe's and certain other retailers had an unfair

competitive advantage as they were not charging sales tax on their sales of built-in dish washers if their customer also orders installation.

In June of 2015, the Department issued a Compliance Alert explaining that an investigation had revealed that some taxpayers were incorrectly treating sales of appliances and other tangible personal property as "construction contracts" and failing to collect and remit ROT on such transactions. The Compliance Alert expressly stated

"The sales of tangible personal property with a separate agreement to install it does not convert the retail sales to a construction contract. This frequently occurs when an appliance is sold, the purchaser requires installation of the appliance, and the invoice lists the charge for installation separately. For example, a person may purchase a dishwasher at an appliance store and the seller and purchaser enter into a separate agreement for the installation of the dishwasher. The seller in this case would pay [sales tax] on the receipts from the sale of the dishwasher."

The Lindbloms further noted that after the Department's issuance of the 2015 Compliance Alert, Lowe's continued to not charge sales tax on installed dishwashers and over-the-range microwaves. The Lindbloms filed this case against Lowe's

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under the Illinois False claims Act alleging that Lowe's knowingly avoided its sales tax obligations and presented the State of Illinois with false monthly use tax returns. The parties agreed to have a trial solely on the issue of liability and address damages at a later trial if needed.

Lowe's provided evidence at trial that its activities fall within the construction contractor provisions as removing the built-in dishwashers or over-the-range microwaves causes damage in the kitchen area, and its sales of such items are in a single contract without a separate installation agreement. Lowe's also submitted supporting evidence during the trial that: 1) its internal Director of Sales and Use Tax conducted a state by state sales tax analysis supporting its use tax treatment; 2) it hired an independent accounting firm to provide guidelines for the sales tax treatment for installed improvements to realty; 3) it retained PwC to consider whether Lowe's was subject to sales or use tax in the context of certain installed sales, and PwC confirmed that built-in dishwashers and over-the range microwaves were subject to Use Tax in Illinois; and 4) the Department performed a sales tax audit of Lowe's activities from January 2008 to June 2010 and did not make any changes to Lowe's application of the construction contractor provisions to its sales of dishwashers and microwaves.

Notwithstanding the evidence Lowe's submitted, the trial court found that Lowe's services of installation were incidental to their retail sales and such sales were subject to sales tax. The trial court also found that Lowe's disregarded the Department's 2015 Compliance Alert, which addressed the sales at issue, resulting in Lowe's violating the Illinois False Claims Act (740 ILCS 175/1 *et seq.*) (West 2022). During the separate trial for damages, the trial court entered a judgment for \$4,148,887 in unpaid sales tax in favor of the Lindbloms as well as attorney fees totaling \$1,321,014.97 and awarded a single penalty of \$11,000. The Lindbloms appealed the amount of damages and attorney fees awarded, and Lowe's appealed the sales tax

liability and violation of the Illinois False Claims Act.

The Illinois Appellate Court begins its analysis of this case by stating that a person violates the Illinois False Claims Act "if they make, use or cause to be made or used, a false record or statement material to an obligation to pay or transmit money to the State, or if the person improperly avoids or decreases an obligation to pay or transmit money to the State," 740 ILCS 175/3(a)(1)(G) (West 2022). The Court adds that in order to prevail under the False Claims Act, the plaintiff must first prove that Lowe's had an obligation to pay sales tax and second, that Lowe's knowingly filed false tax returns.

In addressing the issue of Lowe's obligation to remit sales tax, the Appellate Court needed to determine if the construction contractor exemption applied to Lowe's. The Court explained that the primary or real occupation of the Taxpayer determines the tax classification. The Court determined that Lowe's was not a construction contractor concerning the items at issue as: 1) the overwhelming predominant part of the transaction was the sale of the good at retail not the installation; 2) the cost of the appliance did not change if the appliance was not installed; and 3) Lowe's did not offer installation if the appliance was not purchased at Lowe's. Based on these items, the Court held that Lowe's did not qualify as a "contractor" and was required to collect and remit sales tax for its sales of dishwashers and microwaves with installation.

Since Lowe's was required to collect and remit sales tax, the Appellate Court next addressed whether Lowe's had liability under the Illinois False Claims Act for failing to collect and remit such sales tax. The Appellate Court reversed the trial court and found that for the tax periods prior to the issuance of the 2015 Compliance Alert, Lowe's is not subject to liability under the False Claims Act as it made a good faith effort based on the Illinois statutes and regulations existing at that time, analysis and guidance provided by Lowe's Tax Director and external accounting firms,

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as well as guidance received from the Department during its sales tax audit of Lowe's 2008-2010 transactions.

Notwithstanding, the Appellate Court affirmed the trial court in part by holding that Lowe's was liable under the False Claims Act for tax periods subsequent to the 2015 Compliance Alert. They found that Lowe's did not engage with the same or similar tax experts after the Compliance Alert was issued and appears to have simply disregarded the Compliance Alert and continued to employ the same tax practices as it employed prior to the alert. The Appellate Court added that the alert should have caused Lowe's to revisit its tax practices and that its failure to do so constituted evidence of its desire not to learn about interpretations of the Act and Regulations. Accordingly, for the period beginning in June 2015 after the Department's Compliance Alert was issued, the Appellate Court held that the trial court's finding that Lowe's acted knowingly for purposes of the Illinois False Claims Act was not against the manifest weight of the evidence.

Finally, the Appellate Court remanded the case for a new trial on damages and held that: 1) the Relators are not entitled to damages for the period preceding the issuance of the Department's Compliance Alert, but they are entitled to damages for the period from June 2015 to the point Lowe's was adjudged liable in this case, March 31, 2021; 2) the trial court did not err when it limited the Relator's damages to the State portion of the ROT; 3) the Relators failed to show that the trial court erred or abused its discretion when the trial court denied the Relator's request for an award of prejudgment interest; 4) the trial court should have imposed a penalty for each false record submitted by Lowe's from June 2015 to March 2021—each violation of the Illinois False Claims Act rather than a single \$11,000 penalty; 5) the issue of attorney fees, costs, and expenses should be addressed anew by the trial court on remand; and 6) the trial court erred in trebling the damages before setting off the amount of use tax Lowe's paid during the periods at issue.

This Order was issued just two weeks

after the Home Depot Cook County Circuit Court ruling was issued which addressed another False Claims Act matter and held that Home Depot's underpayment was not subject to the False Claims Act as Home Depot acted reasonably when evaluating its tax position just as Lowe's had prior to the issuance of the Compliance Alert. Of interest with the Lowe's case is that it was initiated by another Illinois taxpayer and business competitor of Lowe's. Based on the holdings in these cases and other cases recently addressed by the Illinois Courts, it appears that the Courts have raised the required level of evidence supporting a tax position and expect Taxpayers to be aware of that heightened expectation when defending or initiating an Illinois tax position.

Please note that the Lowe's Appellate Court Order was filed under Supreme Court Rule 23 and may not be cited as precedent by any party except in their limited circumstances allowed under Rule 23 (e)(1). As of the date of this article, neither party has sought to appeal this matter to the Illinois Supreme Court. ■

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Sonni Choi Williams
ISBA President

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DECEMBER 12-13, 2024 * JW MARRIOTT CHICAGO



Hon. Mary Colleen Roberts
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ILLINOIS BAR FOUNDATION

Champions

Dear Future Champions,

At least twice a year at ISBA Annual and Mid-Year Meetings, we are pitched by colleagues and the Illinois Bar Foundation to become a “Champion.” But what is a Champion really, and what’s in it for us?

A **champion**, by definition, is a person who fights or argues for a cause or on behalf of someone else. As lawyers, we have the unique opportunity to make a positive impact on society by upholding justice and advocating for those in need. We have the power to shape laws, defend the innocent, and ensure fair resolution of disputes. By definition, we are champions, for our clients, our legal system and for our communities, but through the statewide reach of the Illinois Bar Foundation, we have the opportunity to increase our impact even more.

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Sincerely,

Jessica Durkin
Champions Chair
Illinois Bar Foundation

