JONES DAY

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COMMENTARY

The Voluntary Payment Doctrine Defense Is Alive and Well in Illinois

The issue of tax overcollection has triggered a spate of consumer fraud lawsuits (often in the form of class actions) across the country, and it has affected some of the United States' largest corporate businesses. On July 5, 2016, the Appellate Court of Illinois (Fifth District) held that Illinois's voluntary payment doctrine[1] can apply as a defense to the Illinois Consumer Fraud and Deceptive Business Practices Act ("Consumer Fraud Act" or "CFA") (815 ILCS 505/1 *et seq.*). *Karpowicz v. Papa Murphy's Int'l, LLC, et al.*, 2016 IL App (5th) 150320-U (July 5, 2016). While the court's ruling presents a significant defense to tax-remitting businesses in Illinois faced with CFA litigation, it is analytically distinct from other Illinois cases, such as the *Sears* cases discussed below. *Karpowicz* presents the possibility that consumer fraud lawsuits predicated on overcollection of taxes will begin to abate in Illinois and, if other courts view *Karpowicz* as persuasive, perhaps other states and jurisdictions as well.

Background

The plaintiff—purporting to represent a class of similarly situated Illinois residents—filed suit against Papa Murphy's International, LLC (a franchisor that grants franchises for the operation of Papa Murphy's stores) and P-Cubed Enterprises, LLC (a franchisee of Papa Murphy's) after he allegedly paid a $.80 tax on his $9 purchase of a pizza. The Illinois Retailers' Occupation Tax Act provides that a 1 percent tax rate will apply to food items sold by a retailer without facilities for on-premises consumption of food and that are not ready for immediate consumption. The plaintiff alleged that since the pizzas provided by Papa Murphy's are "take-and-bake" and are not ready for consumption, Papa Murphy's 9 percent tax charge was an unfair and deceptive act in violation of the CFA.

The trial court granted the defendants' motions to dismiss, which argued that the plaintiff could not assert a claim to recover taxes that had been remitted to the state, that the suit was barred by the Illinois voluntary payment doctrine, and that the complaint failed to assert a valid claim under the CFA. The plaintiff appealed.

Illinois Voluntary Payment Doctrine Is Applicable to CFA

Under Illinois law, the voluntary payment doctrine bars a consumer from asserting a claim to recover taxes that have been remitted to the state, even if such collection was erroneous.[2] A consumer who wishes to contest the collection of the use tax may do so by

either following the procedure outlined in the Protest Fund Act—i.e., (i) the consumer pays under protest and (ii) then sues the retailer—or by asserting one of the exceptions to the Illinois voluntary payment doctrine. The exceptions to the doctrine are fraud, misrepresentation, or mistake of fact.

The plaintiff claimed that since he alleged statutory fraud, this was an applicable exception to the Illinois voluntary payment doctrine, which should have prohibited the trial court from dismissing his complaint. The Appellate Court rejected the plaintiff's contention on the ground that the plaintiff failed to cite any Illinois law supporting his contention that statutory fraud is an applicable exception; the court also cited to *Jenkins v. Concorde Acceptance Corp*., 802 N.E.2d 1270 (2003) for the proposition that Illinois courts reject the argument that a claim under the CFA is immune from the Illinois voluntary payment doctrine.

How the *Sears* Cases Fit in the Picture

In 2013, the Appellate Court of Illinois (First District) held that the Illinois voluntary payment doctrine is an inapplicable defense to the CFA: "we have established that the defendant's practice of collecting sales tax was not statutorily authorized. If, as the plaintiff alleges, the defendant charged a tax neither it nor the plaintiff was bound to pay, it can be found to have engaged in a deceptive act," thus satisfying the first element of a CFA cause of action. *Nava v. Sears, Roebuck and Co.*, 995 N.E.2d 303, 310 (1st Dist. 2013). Two years later, the First District followed the holding in *Nava* by, this time, affirming the trial court's ruling that the Illinois voluntary payment doctrine is no bar to a cause of action under the CFA. *Aliano v. Sears, Roebuck and Co.*, 48 N.E.3d 1239, 1245, 1249 (1st Dist. 2015).

The distinguishing feature of the *Sears* cases is that the courts found that overcollecting taxes is a deceptive, not an unfair, practice, and that there was sufficient evidence of the defendants' intent to deceive. "Deceptive acts or practices" under the CFA means "'misrepresentation or the concealment, suppression or omission of any material fact, with intent that others rely upon the concealment, suppression or omission of such material fact.'" *Nava*, 995 N.E.2d at 310 (citing 815 ILCS 505/2). The *Nava* court held that since the defendant had a practice of collecting statutorily unauthorized sales taxes that neither it nor the plaintiff was bound to pay, this was sufficient to constitute a deceptive practice. *Id*. Moreover, the court found that there was "substantial evidence that the defendant intended that the plaintiff rely on the deception, as the plaintiff's paying the tax was a natural and predictable consequence of its asking the plaintiff to do so." *Id*.

This analysis varies from the court's analysis in *Karpowicz*, where the court held that simply pleading that the defendants engaged in "an unfair and deceptive practice" without further factual allegations (i.e., pleading unvarnished conclusions) is insufficient to demonstrate intent to deceive. *Karpowicz*, 2016 IL App (5th) 150320-U, ¶ 16. The *Karpowicz* court's reasoning relied on *Jenkins*, which, on an appeal from a motion to dismiss, rejected the plaintiffs' argument that the Illinois voluntary payment defense does not apply to a CFA claim on the basis that the plaintiffs' complaint stated that defendants engaged in an unfair practice, not deception or fraud. *Jenkins*, 802 N.E.2d at 1278. Another reason for the analytical differences between *Nava* and *Karpowicz* is that *Nava* was an appeal of a motion for summary judgment, whereas *Karpowicz* was an appeal of a motion to dismiss; thus the cases applied different legal standards and engaged with differing levels of developed factual records. Consequently, as evidenced from the reasoning in *Karpowicz*, the level of detail in the complaint can affect an Illinois court's finding of a deceptive versus an unfair practice.

As a result, while *Karpowicz* directly supports a defendant's attempt to dismiss a CFA claim under the Illinois voluntary payment doctrine, given the court's analysis, the decision remains distinct from other Illinois cases that have reached different conclusions regarding the application of the Illinois voluntary payment doctrine to a CFA claim. It is likely that the Illinois Supreme Court will get involved to resolve this issue.

Implications

The Illinois voluntary payment doctrine is a valid defense to causes of action in Illinois targeting a company's collection of taxes. More importantly, this issue appears to be one that is ripe for determination by the Illinois Supreme Court. Businesses that collect and remit use tax in Illinois would do well to monitor the development of this issue and consult with their local or in-house counsel to determine the viability of the Illinois voluntary payment doctrine in each specific case.

Lawyer Contacts

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Endnotes

1 The voluntary payment doctrine in Illinois discussed in this *Commentary* limits the ability of a customer to obtain a refund of Illinois tax from the customer's retailer when the retailer has remitted the tax to a taxing authority. This Illinois principle is distinct from the similarly named voluntary payment defense, oft asserted by taxing authorities to deny taxpayers' refund claims. In such situations, the taxing authority alleges the taxpayer failed to pay the now-contested tax under an appropriate form of protest, making the taxpayer's payment "voluntary," and thus barring the taxpayer's refund claim. *See, e.g.*, *Hunt County Tax Appraisal District v. Rubbermaid Inc.*, 719 S.W.2d 215, 218 (Tex. App. 1986), *writ refused NRE* (Jan. 14, 1987) ("It is well settled in Texas law that a person who voluntarily pays an illegal tax has no claim for repayment … This rule is said to be one of sound public policy, the object of which is to discourage litigation and to secure the taxing authority in the orderly conduct of its affairs.") (citations omitted).

2 *See, e.g.*, *Adams v. Jewel Cos.*, 63 Ill. 2d 336, 348-49 (1976); *Hagerty v. General Motors Corp.*, 59 Ill. 2d 52, 59 (1974); *Lusinski v. Dominick's Finer Foods*, 136 Ill. App. 3d 640, 643-44 (1st Dist. 1985).