2011 IL App (4th) 100814-U

Filed 11/4/11

No. 4-10-0814

IN THE APPELLATE COURT

OF ILLINOIS

FOURTH DISTRICT

SOLOMON COLORS, INC., an Illinois Corporation,	)	Appeal from
	)	Circuit Court of
Plaintiff-Appellee,	)	Sangamon County
v.	)	No. 08MR285
THE DEPARTMENT OF REVENUE; BRIAN HAMER, Director of The Department of Revenue; and ALEXI GIANNOULIAS, Treasurer of the State of Illinois,	)	
	)	
	)	Honorable
	)	John W. Belz,
Defendants-Appellants.	)	Judge Presiding.

JUSTICE STEIGMANN delivered the judgment of the court.
Justices Turner and Cook concurred in the judgment.

ORDER

¶ 1 *Held*: The appellate court affirmed the trial court's declaratory judgment and preliminary injunction judgment, concluding that because the plaintiff did not retain ownership in certain containers it used to package and transport its product, the use tax assessed by the defendants was in error.

¶ 2 Following a July 2010 bench trial, the trial court ordered defendants, the State of Illinois, Department of Revenue; Brian Hamer, Director of Revenue; and Alexi Giannoulias, Treasurer of the State of Illinois (collectively, the Department), to return a $30,000 use-tax payment that plaintiff, Solomon Colors, Inc. (Solomon), had tendered to the Department under protest. Specifically, the court found that certain containers Solomon purchased during a three-year period to package and transport its liquid products were not subject to a use tax under the Use Tax Act (35 ILCS 105/1 through 22 (West 2008)).

¶ 3 The Department appeals, arguing that the trial court's finding that the use tax did not apply was against the manifest weight of the evidence. We disagree and affirm.

¶ 4 I. BACKGROUND

¶ 5 A. The Circumstances That Prompted Solomon's Complaint

¶ 6 In April 2008, the Department issued a notice of audit results, informing Solomon, in part, that it owed the state use taxes pursuant to the Use Tax Act. Specifically, the Department concluded that Solomon was subject to a $30,000 use-tax assessment because between 2003 and 2006, Solomon retained ownership of containers–known as "totes"–to package and transport its liquid products to its customers. Solomon later paid the assessment under protest as permitted by section 2a.1 of the State Officers and Employees Money Disposition Act (730 ILCS 225/2a.1 (West 2008)).

¶ 7 In May 2008, Solomon filed a complaint for declaratory judgment and preliminary injunction, seeking a declaratory judgment that the $30,000 tax assessment under the Use Tax Act was contrary to law and void. Later that month, the trial court entered an agreed preliminary injunction order, which enjoined the Department from depositing Solomon's $30,000 payment into the state's general revenue fund or any other state treasury fund.

¶ 8 B. The Evidence Presented by the Parties

¶ 9 After the parties presented their respective opening statements at a July 2010 bench trial on Solomon's suit for preliminary injunction, the trial court sought to clarify the parties' dispute by asking whether the sole issue before the court was Solomon's ownership of the totes. Both parties agreed that if the evidence showed that Solomon retained ownership of the totes after it sold its product, then the use tax would apply. Both parties also agreed that if the

evidence showed that Solomon did not retain ownership of the totes after it sold its product, then the use tax would not apply. Thereafter, the parties presented the following evidence.

¶ 10 1. *The Evidence Presented by Solomon*

¶ 11 Charles Kreutzer, Solomon's executive vice president and chief financial officer, is responsible for Solomon's domestic and international manufacturing and distribution facilities. Kreutzer testified that Solomon manufactures dry powder and liquid colorants that change the naturally gray color of concrete. Solomon packages and sells its colorants–domestically and internationally–in different quantities, which include 10-ounce bottles; 1- to 3- and 1/2-gallon buckets; 600-pound drums, and "totes," which hold up to 4,000 pounds of liquid colorant.

¶ 12 In providing a description of the totes, Kreutzer stated that because the liquid colorant is housed in a 330 gallon, conical-shaped plastic bladder with a dispensing valve, the bladder is supported upright by a metal frame, which is 46 inches square and approximately 66 inches tall. Kreutzer explained that the totes are designed to work with other equipment Solomon manufactures and sells to companies, which (1) automatically dispenses the colorant into the concrete manufacturing process and (2) allows Solomon to efficiently refill the totes.

¶ 13 From January 1, 2003, through December 31, 2006, Solomon purchased totes–that is, the bladder and metal support frames–from an Ohio company for $643 per tote. In doing so, Solomon acknowledged that it did not pay sales tax to the Ohio company on those purchases. Kreutzer explained that with regard to the bottle, bucket, and drum packaging, Solomon "expensed" those items through its "packaging supplies" account, ultimately considering those finished products–including their respective containers–as inventory. Solomon, however, expensed the totes through a separate account so that it could separately track those

expenses.

¶ 14 Kreutzer noted that newly purchased totes were not (1) capitalized as a Solomon asset, (2) marked as Solomon's property, (3) maintained on Solomon's inventory after the colorant was sold, or (4) tracked by customer. In addition, Solomon did not ask its customers to provide a tote security deposit. Kreutzer recounted that he sometimes saw customers reusing totes to store "other chemicals and different things." In some instances, customers would contact Solomon, requesting to return their used totes. Solomon, however, would not retrieve the totes unless enough used totes were in a certain area to justify the retrieval expense.

¶ 15 When Solomon did retrieve used totes, Kreutzer stated that it neither charged nor paid the customer to do so. After retrieving the used totes, Solomon would either (1) dispose of the tote, (2) repair the tote, or (3) clean the tote, depending on its condition. Regardless of the action taken, Solomon did not charge its customer a fee. Additionally, if the tote was repaired, Solomon did not consider the tote as part of its inventory. Kreutzer opined that a tote could be used three or four times without repair but stated that he has seen totes damaged after one use.

¶ 16 Kreutzer acknowledged that when a tote of colorant is sold to a customer, its invoice does not separately list the tote as being sold to the customer but instead, lists the colorant purchase by poundage, color, and the nomenclature for the tote–for example, T-400 tote–which identifies the type of unit to ship to the customer. (The record shows that Solomon uses at least two different types of totes, which it identifies as a T-400 tote and a T-330 tote.)

¶ 17 2. *The Evidence Presented by the Department*

¶ 18 Douglas Moore, a senior auditor, testified that he conducted the audit at issue, which analyzed Solomon's operations between January 2003 to December 2006. Prior to that

audit, Moore stated that Solomon agreed (1) to a "general understanding between the [D]epartment and [Solomon] as far as what the issue was in reference to the totes" and (2) that instead of performing a "complete statistical review," the Department would apply "error rates" derived from the Department's previous audit, which analyzed the period 2000 through 2002. Moore explained that (1) his "general understanding" pertained to "the association of the tote purchasing apart from the other consumables" and (2) he applied the agreed upon error rates to "general purchasing," specifically segregating the tote transactions that occurred from 2003 to 2006 and performing a detailed review of those purchases.

¶ 19 Moore noted that his audit did not focus on the transfer of totes to customers but instead, "the repeated use of the same tote in Illinois for shipping purposes." Moore stated that, during the audit, his conversations with Solomon concerned only the repeated usage of the tote and not the tote's transfer to the customer. In describing the tote, Moore opined, as follows:

> "[T]he tote is used as a vehicle or a means of delivery of a Solomon Colors product for Solomon *** to the customer for multiple reuse. The tote is not transferred. The tote was never intended to be transferred. The tote is used strictly as a vehicle to move product from point A to point B."

¶ 20 In clarifying how his financial analysis supported his opinion regarding the repeated use of the totes, Moore stated the following:

> "Typically, if you have an item that is used for say cost of goods sold, inventory purposes, it is not run as an expense. It is not run as a depreciable asset. You wouldn't see that typically in

the books and records as an expenditure item. If it is a transfer item. Typically, if you have product that is sold say the color pigment or the container that they are in, that's all treated as inventory and it is transferred to the customer as a sale for resale in this particular case."

¶ 21 Moore explained further that he segregated the totes Solomon purchased and used in Illinois from those Solomon purchased and used out of state, by relying on a report generated by an assistant comptroller who tracked tote purchases Solomon made during the 48-month audit period. (The record does not identify whether the assistant comptroller was employed by the Department or Solomon.) Moore then applied the agreed-upon error rates to the totes purchased for use in Illinois. After applying "minor adjustments," Moore calculated a use tax of $30,000.

¶ 22 Moore then identified "Defendants' Exhibit No. 10," which was a copy of a computer-screen image that was provided by Solomon's treasurer and chief financial officer, John Boxman, during the previous audit period and pertained to "questions that were posed to *** Kruetzer, *** Boxman, and Rich Solomon with respect to the usage of the totes." That image, dated September 30, 2003, listed "jboxman" as the "user" and contained the following verbiage:

"A tote costs $643.00. We can use and re-use them about 20 times. With 4,000 lbs. in each tote that would cost out that tote at .0080375 per lbs. On average it costs $55.00 to have a tote returned to Springfield. So $55.00 divided by 4000 lbs = .01375."

¶ 23 Moore testified about exhibit No. 10 as follows:

"Defendant[s'] Exhibit [No.] 10 is a document that was produced for me by *** Boxman on the day of the aforementioned discussion with *** Boxman, *** Kreutzer, and [Rich] Solomon with respect to the usage of the totes. It [was] explained to me that the totes are used indefinitely. There were computations associated with that. This was provided *** to me as a basis of those computations in relationship to how the totes were used, how the totes were accounted *** for accounting purposes, how the totes were costed against products sold. This is a component of the product sell value."

¶ 24 Over Solomon's objection, the trial court admitted into evidence exhibit No. 10, stating the following:

"THE COURT: [The court] will allow it in but [the court] will take it for what it is worth.

*** [T]his is the accountant. You have not shown that [Solomon does] reuse [the totes] 20 times.

[The court] will allow it in for what it is worth."

Based on its admission of exhibit No. 10, the court also admitted, over Solomon's objection, "Defendants' Exhibit No. 9," a "Costed Bill of Material" that Boxman provided during the previous audit period, which showed a computation labeled "Tote Recycle Cost."

¶ 25 Moore acknowledged that with the exception of exhibit Nos. 9 and 10–which pertained to the previous audit period–no documentation existed during the current audit period

that showed Solomon (1) did not intend to transfer the tote simultaneously with the purchase of the colorant, (2) retained ownership of the tote after the sale of the colorant, (3) considered the totes as depreciable assets for accounting purposes, (4) required customers to pay a tote security deposit, (5) placed limitations on customers' use of the tote, or (6) required customers to return the tote after its use. In addition, Moore admitted that he did not have any documentation substantiating that a particular tote was used more than one time, ended up in a landfill, or was used by a customer for alternative purposes.

¶ 26 3. *The Trial Court's Findings*

¶ 27 After the close of evidence, the trial court instructed both parties to file bench briefs, concentrating their efforts on ownership of the tote. In September 2009, the court entered a written judgment, ordering the Department to return the $30,000 use-tax payment Solomon tendered to the Department under protest. Specifically, the court found, in pertinent part, that the totes Solomon had purchased during the three-year period to package and transport its liquid colorants were not subject to a use tax pursuant to the Use Tax Act.

¶ 28 This appeal followed.

¶ 29 II. THE TRIAL COURT'S RULING

¶ 30 The Department argues that the trial court's finding that the use tax did not apply was against the manifest weight of the evidence. Specifically, the Department contends that Solomon did not transfer ownership of the totes at the time it sold its colorant. We disagree.

¶ 31 A. The Standard of Review

¶ 32 We review a trial court's decision following a bench trial to determine whether it was against the manifest weight of the evidence. *Lawlor v. North American Corp. of Illinois*,

409 Ill. App. 3d 149, 171, 949 N.E.2d 155, 178 (2011). The court's judgment is not against the manifest weight of the evidence unless the opposite conclusion is clearly evident. *Id.*

¶ 33 A. The Applicable Statutory Scheme Regarding the Use Tax

¶ 34 Section 3 of the Use Tax Act provides, in pertinent part, as follows:

> "A tax is imposed upon the privilege of using in this State tangible personal property purchased at retail from a retailer[.]" 35 ILCS 105/3 (West 2008).

¶ 35 Section 2 of the Use Tax Act provides, in part, the following definitions:

> " 'Use' means the exercise by any person of any right or power over tangible personal property incident to the ownership of that property, *except that it does not include the sale of such property in any form as tangible personal property in the regular course of business to the extent that such property is not first subjected to a use for which it was purchased,* and does not include the use of such property by its owner for demonstration purposes: Provided that the property purchased is deemed to be purchased for the purpose of resale, despite first being used, to the extent to which it is resold as an ingredient of an intentionally produced product or by-product of manufacturing.
>
> * * *
>
> 'Sale at retail' means any transfer of the ownership of or title to tangible personal property to a purchaser, for the purpose of

use, and not for the purpose of resale in any form as tangible personal property to the extent not first subjected to a use for which it was purchased, for a valuable consideration: Provided that the property purchased is deemed to be purchased for the purpose of resale, despite first being used, to the extent to which it is resold as an ingredient of an intentionally produced product or by-product of manufacturing." (Emphases added.) 35 ILCS 105/2 (West 2008).

¶ 36 Section 3-65 of the Use Tax Act provides as follows:

"If the seller of tangible personal property for use would not be taxable under the Retailers' Occupation Tax Act [(35 ILCS 120/1 through 14 (West 2008)),] despite all elements of the sale occurring in Illinois, then the tax imposed by this Act does not apply to the use of the tangible personal property in this State." 35 ILCS 105/3-65 (West 2008).

¶ 37 Section 130.2070(b)(1) of title 86 of the Illinois Administrative Code, entitled, "Sales of Containers, Wrapping and Packing Materials and Related Products," provides as follows:

"Sellers of containers to purchasers who sell tangible personal property contained in such containers to others are deemed to make sales of such containers to purchasers for purposes of resale, the receipts from which sales are not subject to the

> Retailers' Occupation Tax, if the purchasers of such containers transfer the ownership of the containers to their customers together with the ownership of the tangible personal property contained in such containers." 86 Ill. Adm. Code 130.2070(b)(1), amended at 24 Ill. Reg. 15104 (eff. Oct. 2, 2000).

¶ 38 B. Ownership of the Totes

¶ 39 The Department asserts that "it is undisputed that the sole issue in this case is whether Solomon *** intended to transfer ownership of the totes to its customers during the relevant audit period (2003-2006)." In support of its contention that Solomon did not transfer ownership of the totes at the time it sold its colorant to its customers, the Department primarily relies on (1) exhibit No. 9 to show that Solomon charged their customers a "tote recycle fee" and (2) exhibit No. 10 to show that Solomon reused the tote about 20 times. Indeed, citing to exhibit No. 10 in its brief to this court, the Department claims that "the lynchpin in this case is Solomon's concession that it intended to use and reuse the totes, not resell them."

¶ 40 The record, however, shows that despite the Department's reliance, exhibit Nos. 9 and 10 concerned information Solomon provided to the Department during the prior audit period, which analyzed Solomon's business operations during calendar years 2000 through 2002, not the four-year time period of the audit before us–that is, 2003 through 2006–for which the $30,000 use tax was assessed. Notwithstanding this discrepancy, the Department claims that the evidence presented showed that Solomon did not transfer ownership of the totes to its purchasing customers in that Solomon (1) used the totes solely as a means to transfer its colorant, (2) retrieved totes from its customers and reused them to sell colorant to other customers, (3) did not

separately itemize the totes on its invoices, and (4) charged its customers a tote recycle fee, which demonstrated that it intended to reuse the totes up to 20 times. Despite the Department's claim, however, our review concerns whether the evidence presented clearly mandates the opposite conclusion reached by the trial court. In this regard, we conclude that it does not.

¶ 41 In this case, the record shows that in addition to Moore's testimony and exhibit Nos. 9 and 10, the trial court also considered Kruetzer's testimony, which showed that the newly purchased totes were not (1) capitalized as a Solomon asset, (2) marked as Solomon's property, (3) maintained on Solomon's inventory after the colorant was sold, or (4) tracked by customer. Indeed, as Moore confirmed, documentation did not exist during the relevant reporting period to show that Solomon (1) did not intend to transfer the tote simultaneously with the purchase of the colorant, (2) retained ownership of the tote after the sale of the colorant, (3) considered the totes as depreciable assets for accounting purposes, (4) required customers to pay a tote security deposit, (5) placed limitations on customers' use of the tote, or (6) required customers to return the tote after its use. In other words, absent exhibit Nos. 9 and 10–which pertained to the previous audit period–the evidence presented showed that during the 2003 through 2006 audit period, Solomon sold totes of colorants, intending to transfer ownership of those respective totes to its customers.

¶ 42 Accordingly, given the evidence presented and our standard of review, we conclude that the trial court's judgment was not against the manifest weight of the evidence.

¶ 43 In so concluding, we note that despite the Department's claim that the sole issue before us concerned ownership of the totes, the Department also argued that Solomon failed to present any evidence that it tendered to the Ohio company from which it purchased the totes a

Certificate of Resale as suggested by section 130.1405 of title 86 of the Administrative Code, entitled, "Seller's Responsibility to Obtain Certificates of Resale and Requirements for Certificate of Resales." 86 Ill. Adm. Code 130.1405, amended at 24 Ill. Reg. 15104 (eff. Oct. 2, 2000). Thus, the Department claims that Solomon failed to overcome the "presumption that the totes were not purchased for resale but, instead, were purchased for use in Illinois."

¶ 44 Our review of section 130.1405 of title 86 of the Code, however, shows that a Certificate of Resale is a statement signed by the purchaser–in this case Solomon–that the property purchased is purchased for purposes of resale. 86 Ill. Adm. Code 130.1405(b), amended at 24 Ill. Reg. 15104 (eff. Oct. 2, 2000). Section 130.1405(a) of title 86 of the Code suggests that sellers–which in this case would be the Ohio company, "should, for their protection, take a Certificate of Resale from the purchaser." 86 Ill. Adm. Code 130.1405(a), amended at 24 Ill. Reg. 15104 (eff. Oct. 2, 2000). Not doing so "creates a presumption that a sale is not for resale." 86 Ill. Adm. Code 130.1405(d), amended at 24 Ill. Reg. 15104 (eff. Oct. 2, 2000). "*This presumption may be rebutted by other evidence that all of the seller's sales are sales for resale*." (Emphasis in original.) 86 Ill. Adm. Code 130.1405(d), amended at 24 Ill. Reg. 15104 (eff. Oct. 2, 2000). Therefore, because section 130.1405 applies to the seller, which in this case would be an Ohio company that is not subject to the tax laws of this State, we reject the Department's claim that Solomon failed to overcome the presumption that the totes were not purchased for resale.

¶ 45 III. CONCLUSION

¶ 46 For the reasons stated, we affirm the trial court's declaratory judgment and preliminary injunction judgment.

¶ 47 Affirmed.