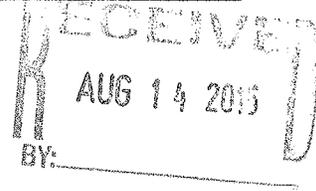


IN THE ILLINOIS INDEPENDENT TAX TRIBUNAL

KOCH INDUSTRIES, INC. )  
 )  
 Petitioner, )  
 )  
 v. )  
 )  
 ILLINOIS DEPARTMENT )  
 OF REVENUE )  
 )  
 Respondent. )

No. \_\_\_\_\_



15 TT 170

PETITION

The Petitioner, Koch Industries, Inc. ("Petitioner"), individually and on behalf of its unitary affiliates, by and through its attorneys, Baker & McKenzie LLP, who are duly authorized to represent Petitioner in this regard pursuant to the Power of Attorney attached hereto as Exhibit A, hereby petitions the Illinois Independent Tax Tribunal to review and reverse the Notices of Deficiency issued by the Illinois Department of Revenue ("Department") as follows:

PARTIES

- 1. Petitioner is a corporation with its principal place of business in Wichita, Kansas.
- 2. Petitioner's federal identification number is 48-0484227.
- 3. Petitioner's address is 4111 E. 37<sup>th</sup> Street N. Wichita Kansas 67220-3203, and its telephone number is 316-828-5500.
- 4. Respondent is an agency of the State of Illinois responsible for administering and enforcing the revenue laws of the State of Illinois.

JURISDICTION

- 5. The Department issued Notices of Deficiency ("Notices") on June 17, 2015 assessing corporation income tax, penalty and interest for 2010 and 2011, letter IDs

CNXXX13645X26728 and CNXXX11832X66721 respectively. Copies of the Notices are attached hereto as Exhibit B.

6. This Tribunal has original jurisdiction over all Department determinations reflected on Notices of Deficiency, among other notices, where the amount at issue exceeds \$15,000, exclusive of penalties and interest. 35 ILCS 1010/1-45.
7. The amount at issue in this matter exceeds \$15,000 exclusive of penalties and interest such that this Tribunal has original jurisdiction over the matter.

### **BACKGROUND**

8. The Department audited Petitioner's 2010 and 2011 corporation income tax returns.
9. Based on its audit, the Department adjusted Petitioner's deductions for certain related party expenses.
10. Specifically, the Department adjusted the amount of affiliated company interest expense exempt from addition modification and properly deductible.
11. Based on this adjustment, the Department issued the Notices at issue.

### **COUNT I**

12. The Department's adjustment overstates Petitioner's related party expense addition by understating the amount of affiliated company interest expense that is exempt from addition modification.
13. Illinois law requires taxpayers to add back to taxable income certain identified related party expenses, including affiliated interest. 35 ILCS 5/203.
14. This adjustment is required for interest paid to a foreign entity if that entity would be included in the unitary business group but for the fact that more than 80% of the business activity is outside of the United States. 35 ILCS 5/203(b)(2)(E-12).

15. Illinois law, namely 35 ILCS 5/203(b)(2)(E-12), provides several exemptions to the addition modification including, but not limited to, when the interest:

- (i) Is paid to an entity subject in a foreign country to a tax measured by net income;
- (ii) When the taxpayer can establish based on clear and convincing evidence that the interest paid relates to an agreement entered into at arm's-length rates and terms and the principal purpose for the payment is not federal or Illinois tax avoidance; or
- (iii) When the taxpayer can establish by clear and convincing evidence that the adjustments are unreasonable.

16. The Department erroneously adjusted the addition modification by not allowing one or more exemptions for which Petitioner qualifies.

17. Under 35 ILCS 5/203(b)(2)(E-12)(i), Petitioner paid interest to an entity subject in a foreign country to a tax measured by net income.

18. Under 35 ILCS 5/203(b)(2)(E-12)(iii), Petitioner's debt agreements were entered into at arm's-length rates and terms and the principal purpose of such agreements and payment of interest was not federal or Illinois tax avoidance.

19. Under 35 ILCS 5/203(b)(2)(E-12)(iv), the application of Illinois addition modification to Petitioner's related party interest expense is unreasonable.

20. Petitioner qualifies for other exemptions to the addition modification provided under 35 ILCS 5/203(b)(2)(E-12) and Illinois law.

21. The Department's denial of Petitioner's affiliated company interest expense deductions is in error and must be reversed.

WHEREFORE, Petitioner prays the Tax Tribunal enter an order abating the Notices in their entirety and such other and further relief as the Tax Tribunal deems appropriate in this matter.

## COUNT II

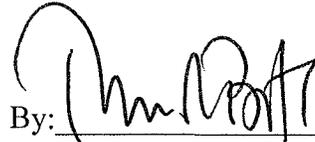
22. Petitioner hereby restates and realleges the allegations contained in paragraphs 1 through 21 as if fully set forth herein.
23. In the alternative, although the Department's adjustment to Petitioner's amount of affiliated company interest expense exempt from addition modification is in error, if upheld, penalties must be abated.
24. The Department's assessment imposes UPIA-5 late payment penalty for 2010 and 2011 in the amounts specified in the notices.
25. The Department's assessment of penalties must be abated for reasonable cause.
26. Under Illinois law, no penalties shall be imposed on a taxpayer if his failure to pay tax was due to reasonable cause. 35 ILCS 735/3-8.
27. Under Illinois regulations, "the most important factor to be considered in making a determination to abate a penalty will be the extent to which the taxpayer made a good faith effort to determine his proper tax liability and to file and pay his proper liability in a timely fashion." 86 ILAC § 700.400(b).
28. A taxpayer is considered to have made a good faith effort to determine and file and pay his tax liability if "he exercised ordinary business care and prudence in doing so." 86 ILAC § 700.400(c).
29. The taxpayer's filing history is also considered in determining whether the taxpayer acted in good faith. 86 ILAC § 700.400(d).

30. Petitioner made a good faith effort to comply with all applicable laws in preparing the tax returns and timely submitting the tax due and was not reckless, careless or negligent in doing so.
31. Petitioner exercised ordinary business care and prudence in determining its proper tax liability and filing and paying its proper liability in a timely fashion.
32. Petitioner has a history of timely filing Illinois corporate income tax returns and paying Illinois corporate income tax in a timely manner.
33. Assessment of penalty is not appropriate where the assessment of tax results from reasonable differences or opinions as to the tax liability.
34. Reasonable differences exist here such that even if assessment of the tax at issue is appropriate, assessment of penalty is not.
35. The UPIA-5 late payment penalties imposed by the Department must be abated for reasonable cause.

WHEREFORE, Petitioner prays the Tax Tribunal enter an order that any penalties assessed by the Department be abated in full and such other and further relief as the Tax Tribunal deems appropriate in this matter.

(The remainder of this page is intentionally blank. Signature page follows.)

Koch Industries, Inc.

By: 

\_\_\_\_\_  
An Attorney for Petitioner

Date: August 14, 2015

Theodore R. Bots (Theodore.Bots@Bakermckenzie.com)  
Roman P. Patzner (Roman.Patzner@Bakermckenzie.com)  
Baker & McKenzie LLP  
300 East Randolph Street, Suite 5000  
Chicago, Illinois 60601  
312-861-8000  
Attorney No. 90080  
3554779-v5\

# **EXHIBIT A**



# IL-2848 Power of Attorney

## Read this information first

Attach a copy of this form to each specific tax return or item of correspondence for which you are requesting power of attorney. **Do not send this form separately.**

### Step 1: Complete the following taxpayer information

1 <u>Koch Industries, Inc.</u> Taxpayer's name	3 <u>4111 E. 37th Street N.</u> Taxpayer's street address		
2 <u>48-0484227</u> Taxpayer's identification number(s)	<u>Wichita</u> City	<u>KS</u> State	<u>67220</u> ZIP

### Step 2: Complete the following information

4 The taxpayer named above appoints the following representatives as attorneys-in-fact:

<u>Theodore R. Bots</u> Name	<u>Roman P. Patzner</u> Name	<u></u> Name
<u>Baker &amp; McKenzie LLP</u> Name of firm	<u>Baker &amp; McKenzie LLP</u> Name of firm	<u></u> Name of firm
<u>300 East Randolph, Suite 5000</u> Street address	<u>300 East Randolph, Suite 5000</u> Street address	<u></u> Street address
<u>Chicago</u> <u>IL</u> <u>60601</u> City State ZIP	<u>Chicago</u> <u>IL</u> <u>60601</u> City State ZIP	<u></u> <u></u> <u></u> City State ZIP
<u>( 312 ) 861-8845</u> Daytime phone number	<u>( 312 ) 861-8945</u> Daytime phone number	<u>( )</u> Daytime phone number
<u>Theodore.Bots@bakermckenzie.com</u> E-mail address	<u>Roman.Patzner@bakermckenzie.com</u> E-mail address	<u></u> E-mail address
<u>Corporate Income Tax</u> <u>2010/11</u> Specific tax type Year or period	<u>Corporate Income Tax</u> <u>2010/11</u> Specific tax type Year or period	<u></u> <u></u> Specific tax type Year or period

5 The attorneys-in-fact named above shall have, subject to revocation, full power and authority to perform any act that the principals can and may perform, including the authority to receive confidential information.

The attorneys-in-fact named above **do not** have the power to – *Check only the items below you do not wish to grant.*

- endorse or collect checks in payment of refunds.
- receive checks in payment of any refund of Illinois taxes, penalties, or interest.
- execute waivers (including offers of waivers) of restrictions on assessment or collection of deficiencies in tax and waivers of notice of disallowance of a claim for credit or refund.
- execute consents extending the statutory period for assessments or collection of taxes.
- delegate authority or substitute another representative.
- file a protest to a proposed assessment.
- execute offers in compromise or settlement of tax liability.
- represent the taxpayer before the Illinois Department of Revenue in all proceedings including hearings (requiring representation by an attorney) pertaining to matters specified above.
- obtain a private letter ruling on behalf of the taxpayer.
- perform other acts (explain) \_\_\_\_\_

6 This power of attorney revokes all prior powers of attorney on file with the Illinois Department of Revenue with respect to the same matters and years or periods covered by this form, except for the following:

<u></u> Name	<u></u> Name	<u></u> Name
<u></u> Street address	<u></u> Street address	<u></u> Street address
<u></u> <u></u> <u></u> City State ZIP	<u></u> <u></u> <u></u> City State ZIP	<u></u> <u></u> <u></u> City State ZIP
<u></u> Daytime phone number	<u></u> Daytime phone number	<u></u> Daytime phone number
<u></u> Date granted	<u></u> Date granted	<u></u> Date granted



7 Copies of notices and other written communications addressed to the taxpayer in proceedings involving the matters listed on the front of this form should be sent to the following:

Theodore R. Bots, Baker & McKenzie

Name

300 East Randolph, Suite 5000

Street address

Chicago IL 60601

City State ZIP

(312) 861-8845

Daytime phone number

Name

Street address

City State ZIP

( )

Daytime phone number

Name

Street address

City State ZIP

( )

Daytime phone number

### Step 3: Taxpayer's signature

If signing as a corporate officer, partner, fiduciary, or individual on behalf of the taxpayer, I certify that I have the authority to execute this power of attorney on behalf of the taxpayer.

_____ Taxpayer's signature	_____ Title, if applicable	_____ Date
<u><i>[Signature]</i></u> Spouse's signature	<u>Senior Vice President- Tax</u> Title, if applicable	<u>August 13, 2015</u> Date
_____ If corporation or partnership, signature of officer or partner	_____ Title, if applicable	_____ Date

### Step 4: Complete the following if the power of attorney is granted to an attorney, a certified public accountant, or an enrolled agent

I declare that I am **not** currently under suspension or disbarment and that I am

- a member in good standing of the bar of the highest court of the jurisdiction indicated below; or
- duly qualified to practice as a certified public accountant in the jurisdiction indicated below; or
- enrolled as an agent pursuant to the requirements of United States Treasury Department Circular Number 230.

<u>Attorney</u>	<u>IL</u>	<u><i>[Signature]</i></u>	<u><i>[Signature]</i></u>
Designation (attorney, C.P.A., enrolled agent)	Jurisdiction (state(s), etc.)	Signature	Date
<u>Attorney</u>	<u>IL</u>	<u><i>[Signature]</i></u>	<u>8/14/15</u>
Designation (attorney, C.P.A., enrolled agent)	Jurisdiction (state(s), etc.)	Signature	Date
_____ Designation (attorney, C.P.A., enrolled agent)	_____ Jurisdiction (state(s), etc.)	_____ Signature	_____ Date

### Step 5: Complete the following if the power of attorney is granted to a person other than an attorney, a certified public accountant, or an enrolled agent

If the power of attorney is granted to a person other than an attorney, a certified public accountant, or an enrolled agent, this document must be witnessed or notarized below. Please check and complete one of the following.

Any person signing as or for the taxpayer

\_\_\_\_\_ is known to and this document is signed in the presence of the two disinterested witnesses whose signatures appear here.

\_\_\_\_\_  
Signature of witness Date

\_\_\_\_\_  
Signature of witness Date

\_\_\_\_\_ appeared this day before a notary public and acknowledged this power of attorney as his or her voluntary act and deed.

\_\_\_\_\_  
Signature of notary Date

**Notary seal**



# **EXHIBIT B**

# Notice of Deficiency

for Form IL-1120, Corporation Income and Replacement Tax Return



June 17, 2015



Letter ID: CNXXX13645X26728

Taxpayer ID: 48-0484227  
Reporting period: December 2010  
Total Deficiency: \$493,525.88  
Balance due: \$493,525.88

\_\_\_\_\_  
#BWNKMGV  
#CNXX X136 45X2 6728#  
KOCH INDUSTRIES INC  
4111 E 37TH ST N  
\_\_\_\_\_  
WICHITA KS 67220-3203  
\_\_\_\_\_



We have audited your account for the reporting period listed above. The attached statement explains the computation of your deficiency and the balance due. **Illinois law requires that we notify you of this deficiency and your rights.**

**If you agree to this deficiency**, pay the total balance due as soon as possible to minimize penalty and interest assessed. Make your check payable to "Illinois Department of Revenue," write your taxpayer ID on your check, and mail a copy of this notice along with your payment.

**If you do not agree, you may contest this notice by following the instructions listed below.**

- **If the amount of this tax deficiency, exclusive of penalty and interest is more than \$15,000, or if no tax deficiency is assessed but the total penalties and interest are more than \$15,000**, file a petition with the Illinois Independent Tax Tribunal within **60 days** of this notice. Your petition must be in accordance with the rules of practice and procedure provided by the Tribunal (35 ILCS 1010/1-1, *et seq.*).
- **In all other cases**, file a protest with us, the Illinois Department of Revenue, within **60 days** of this notice. If you file a protest on time, we must reconsider the proposed deficiency, and if requested, grant you or your authorized representative an administrative hearing. An administrative hearing is a formal legal proceeding conducted pursuant to rules adopted by the Department and is presided over by an administrative law judge. Submit your protest on Form EAR-14, Format for Filing a Protest for Income Tax, (available on our website at [tax.illinois.gov](http://tax.illinois.gov)). If we do not receive your protest within **60 days**, this deficiency will become final. A protest of this notice does not preserve your rights under any other notice.
- **In any case**, you may instead, under Sections 2a and 2a.1 of the State Officers and Employees Money Disposition Act (30 ILCS 230/2a, 230/2a.1), pay the total deficiency under protest using Form RR-374, Notice of Payment Under Protest (available on our website at [tax.illinois.gov](http://tax.illinois.gov)), and file a complaint with the circuit court for a review of our determination.

If you do not protest this notice or pay the balance due in full, we may take collection action against you for the balance due, which may include levy of your wages and bank accounts, filing of a tax lien, or other action.

If you have questions, call us at the telephone number shown below.

Sincerely,

Constance Beard  
Director

ILLINOIS DEPARTMENT OF REVENUE  
AUDIT BUREAU  
PO BOX 19012  
SPRINGFIELD IL 62794-9012

(217) 524-5292

**REDACTED**

# Notice of Deficiency

for Form IL-1120, Corporation Income and Replacement Tax Return



June 17, 2015



Letter ID: CNXXX11832X66721

\_\_\_\_\_  
#BWNKMGV  
#CNXX X118 32X6 6721#  
KOCH INDUSTRIES INC  
4111 E 37TH ST N  
WICHITA KS 67220-3203

**Taxpayer ID:** 48-0484227  
**Audit ID:** A1210075136  
**Reporting period:** December 2011  
**Total Deficiency:** \$3,798,548.19  
**Balance due:** \$3,259,887.40



We have audited your account for the reporting period listed above. The attached statement explains the computation of your deficiency and the balance due. **Illinois law requires that we notify you of this deficiency and your rights.**

**If you agree to this deficiency**, pay the total balance due as soon as possible to minimize penalty and interest assessed. Make your check payable to "Illinois Department of Revenue," write your taxpayer ID on your check, and mail a copy of this notice along with your payment.

**If you do not agree, you may contest this notice by following the instructions listed below.**

- **If the amount of this tax deficiency, exclusive of penalty and interest is more than \$15,000, or if no tax deficiency is assessed but the total penalties and interest are more than \$15,000**, file a petition with the Illinois Independent Tax Tribunal within **60 days** of this notice. Your petition must be in accordance with the rules of practice and procedure provided by the Tribunal (35 ILCS 1010/1-1, *et seq.*).
- **In all other cases**, file a protest with us, the Illinois Department of Revenue, within **60 days** of this notice. If you file a protest on time, we must reconsider the proposed deficiency, and if requested, grant you or your authorized representative an administrative hearing. An administrative hearing is a formal legal proceeding conducted pursuant to rules adopted by the Department and is presided over by an administrative law judge. Submit your protest on Form EAR-14, Format for Filing a Protest for Income Tax, (available on our website at [tax.illinois.gov](http://tax.illinois.gov)). If we do not receive your protest within **60 days**, this deficiency will become final. A protest of this notice does not preserve your rights under any other notice.
- **In any case**, you may instead, under Sections 2a and 2a.1 of the State Officers and Employees Money Disposition Act (30 ILCS 230/2a, 230/2a.1), pay the total deficiency under protest using Form RR-374, Notice of Payment Under Protest (available on our website at [tax.illinois.gov](http://tax.illinois.gov)), and file a complaint with the circuit court for a review of our determination.

If you do not protest this notice or pay the balance due in full, we may take collection action against you for the balance due, which may include levy of your wages and bank accounts, filing of a tax lien, or other action.

If you have questions, call us at the telephone number shown below.

Sincerely,

Constance Beard  
Director

ILLINOIS DEPARTMENT OF REVENUE  
AUDIT BUREAU  
PO BOX 19012  
SPRINGFIELD IL 62794-9012

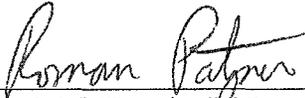
(217) 524-5292

**REDACTED**

## CERTIFICATE OF SERVICE

I hereby certify that on August 14, 2015 a copy of the foregoing Petition has been duly served by U.S. mail, first-class, postage prepaid, on the Illinois Department of Revenue at the following address:

Illinois Department of Revenue  
Office of Legal Services  
100 W. Randolph St., Level 7-900 (7<sup>th</sup> Floor Thompson Center)  
Chicago, Illinois 60601



---

Baker & McKenzie, LLP  
300 East Randolph Street, Suite 5000  
Chicago, Illinois 60601  
312-861-8000