

**ILLINOIS INDEPENDENT
TAX TRIBUNAL**

O&S CORP. d/b/a CITGO,)	
Petitioner,)	
)	
v.)	14 TT 151
)	Chief Judge James M. Conway
ILLINOIS DEPARTMENT)	
OF REVENUE,)	
Respondent.)	

ORDER ON PETITIONER’S MOTION IN LIMINE

O&S Corp. is seeking to preclude the admission of certain records into evidence at its final hearing before the Tax Tribunal. It claims that tax return information and return information from the Indiana Department of Revenue which was used by an Illinois Department of Revenue’s auditor to analyze and compute an Indiana-based vendor’s sales of tobacco products to O&S is impermissible hearsay and cannot be admitted as business records under Illinois Rule of Evidence 803(6).

The Department argues that the records provided by the Indiana Department of Revenue meet the requirements of Rule 803(6) and offers Illinois Rule of Evidence 803(8)- the Public Records hearsay exception, the Illinois Administrative Procedures Act Section 100/10-40, and Sections 5 and 8 of the Illinois Retailers’ Occupation Tax Act as additional legal authority for the admissibility of the those records.

Factual Background¹

O&S operates a Citgo-branded gasoline station at 10007 South Michigan Ave. in Chicago, Illinois. The gas station includes a convenience store where it sells a variety of products, including “other tobacco products” also known as OTP.² Beginning in 2013, an audit was conducted by the Illinois Department of Revenue to determine the amount of OTP sold at the gas station because those types of products are subject to taxation pursuant to the Illinois Tobacco Products Tax Act of 1995 found at 35 ILCS 143/3-5, *et seq.*

Despite selling OTP at the gas station during the relevant audit period, O&S did not file any Tobacco Products Tax Returns. Generally, retail sellers of OTP, like O&S, do not have to file those returns or pay a tax if the product they sell was purchased by them from a wholesaler who otherwise paid the tax. However, O&S purchased some of its OTP from My Enterprise, Inc. (“MEI”), an Indiana-based wholesaler, who did not pay Illinois Tobacco Tax on its OTP sales to O&S.

As part of the Illinois audit of O&S, the auditor obtained records of tax returns and tax return information from the Indiana Department of Revenue relating to MEI.³ The Indiana records reflected sales to O&S of OTP from MEI on a monthly basis over a 53 month period with the notable exception of four months for which there are no records of sales transactions. According to the Illinois Department of Revenue, its auditor estimated OTP sales from MEI to O&S for the missing four months by projecting sales based on the 49 months for which there were records.

During the Illinois audit of O&S, records were provided by O&S for its purchases of OTP. A box of invoices purporting to contain all the purchase invoices for OTP was given to the auditor, but it did not contain any invoices relating to MEI. At some point in the audit, the Illinois auditor was provided several MEI invoices from O&S which the Illinois auditor tied into the schedules of sales from MEI to O&S that were obtained from Indiana. An additional informal ledger was

¹ This factual background is gleaned from the various filings in this case including the pending motion and response. No hearing has been held to test the allegations and the credibility of the witnesses, or to attach weight to the specific items of evidence.

² OTP includes, but is not limited to, cigars, cheroots, stogies, chewing tobacco, snuff, and twist tobacco.

³ That information included “...actual MEI direct information received and originally maintained by the Ind. Department.” Dept.’s Response at 5. That direct information includes returns and schedules from MEI. *Id.* at 10. According to the Department, over 90% of the assessment at issue was based on actual Ind. Department return schedule information with the remaining portion based on estimated projections from the actual return schedule information. *Id.* at 6.

provided by O&S to the Illinois auditor which had additional suppliers listed for purchases of OTP. Because no purchases from MEI were reflected in the books and records of O&S, save the few invoices provided by it after the audit began, the Illinois auditor determined the books and records of O&S were inaccurate and did not rely upon them to determine the OTP purchases of O&S. The auditor determined the amount of OTP bought by O&S from MEI by accepting the figures provided by Indiana and by making several monthly estimates for the four months for which there were no records. Based on the additional purchases, the auditor was able to determine additional sales of OTP on which tobacco tax should have been paid.

Turning to the present, despite the Illinois auditor reviewing several MEI invoices that were provided by O&S during the audit, those invoices have not been forthcoming from O&S or from the Department during the proceedings before the Tax Tribunal and are presumed missing. Neither side has produced any underlying records from MEI which could be used to validate the Department's calculations.

The Department's calculation of tobacco tax is deemed to be *prima facie* correct. 35 ILCS 5/904(a). O&S has the burden to come forward with competent evidence of proving the assessment to be incorrect. *See Copilevitz v. Dep't of Revenue*, 41 Ill. 2d. 154, 156-157 (1968). O&S claims that the Indiana records of MEI sales to O&S are inherently unreliable, particularly in light of the fact that there are no MEI invoices presently available to test those records. O&S further argues that the records were based on information provided by MEI to the Indiana authorities and MEI had a motive to falsify that information and increase its purported sales to Illinois-based retailers in order to escape Indiana sales tax. O&S seeks to preclude admission of the Indiana Department of Revenue records which reflect MEI sales to O&S in its final hearing before the Tribunal by claiming those records are not qualified business records which could be admitted pursuant to Illinois Rule of Evidence 803(6).⁴

⁴ In the O&S petition filed on August 4, 2014 filed by previous counsel for O&S, O&S admitted that it had purchased OTP from MEI, admitted that it had purchased OTP from MEI for the relevant months at issue save for the few months for which the Indiana Department of Revenue did not have information that reflected any MEI/ O&S transactions, admitted it produced MEI invoices during the Illinois Department of Revenue's audit and that those invoices matched up to the Indiana Department of Revenue's information.

Legal Analysis

Illinois Rule of Evidence 803(6) provides:

(6) Records of Regularly Conducted Activity. A memorandum, report, record, or data compilation, in any form, of acts, events, conditions, opinions, or diagnoses, made at or near the time by, or from information transmitted by, a person with knowledge, if kept in the course of a regularly conducted business activity, and if it was the regular practice of that business activity to make the memorandum, report, record or data compilation, all as shown by the testimony of the custodian or other qualified witness, or by certification that complies with Rule 902(11), unless the source of information or the method or circumstances of preparation indicate lack of trustworthiness, but not including in criminal cases medical records. The term “business” as used in this paragraph includes business, institution, association, profession, occupation, and calling of every kind, whether or not conducted for profit.

O&S is correct that the records obtained from the Indiana Department of Revenue are not admissible under Rule 803(6) as those records were not made as part of a regularly conducted business operation at that agency. Rule 803(6) operates as a gatekeeping function for routine business records which allows the admission of records for a business when it can be demonstrated that the records were created at or near the time of the events reflected on the records and that it was the routine business of that business to create those specific records. While Rule 803(6)’s requirements are flexible to allow the admission of virtually all business records, records from a public agency, like revenue departments, do not fit precisely under Rule 803(6). For example, purchase invoices from MEI to O&S are properly admissible under Rule 803(6) assuming the foundation for such records are provided by a custodian of records from MEI under Ill. R. Evid. 902(11). Those same invoices, if provided to a revenue department, cannot be said to have been created during the course of that department’s business. However, the analysis to determine the admissibility of the Indiana Department of Revenue’s doesn’t stop there.

Illinois Rule of Evidence Rule 803(8) provides:

(8) Public Records and Reports. Records, reports, statements, or data compilations, in any form, of public offices or agencies, setting forth (A) the activities of the office or agency, or (B) matters observed pursuant to duty imposed by law as to which matters there was a duty to report, excluding, however, police accident reports and in criminal cases medical records and matters observed by police officers and other law enforcement personnel, unless the sources of information or other circumstances indicate lack of trustworthiness.

The records of the Indiana Department of Revenue at issue in this case consist of records, reports and data compilations made or obtained during the course of the regularly conducted activity of that public agency. That agency relies on records provided to it by taxpayers and through its own creation of internal records, including audit reports, which are then used by that agency to conduct the regular operations of that agency. Those types of documents fall squarely under Rule 803(8) and are admissible at O&S's final hearing under that Rule.⁵

The Illinois Department of Revenue also argues that the Indiana Department of Revenue records are admissible under Sections 5 and 8 of the Illinois Retailers' Occupation Tax which can be found at 35 ILCS 120/5-1 and 8. The Department cites to that portion of Section 5 which allows for the introduction into evidence of Department records in a situation where a taxpayer fails to file a return. *See* Dep't Response at 11.

35 ILCS 120/5-1, reads, in part:

In case any person engaged in the business of selling tangible personal property at retail fails to file a return, the Department shall determine the amount of tax due from him according to its best judgment and information, which amount so fixed by the Department shall be prima facie correct and shall be prima facie evidence of the correctness of the amount of tax due, as shown in

⁵ In making its 803(6) argument, O&S claims that records supplied to the Indiana Department of Revenue by MEI are inherently suspect and unreliable as MEI had a motive to increase tobacco sales to Illinois-based retailers in order to escape taxation by the Indiana authorities on its Indiana-based sales. It is presumed that taxpayers file correct information as opposed to knowingly filing false information with taxing authorities. O&S argument is pure unfounded speculation at this point and is rejected.

such determination. ... Proof of such determination by the Department may be made at any hearing before the Department or in any legal proceeding by a reproduced copy or computer print-out of the Department's record relating thereto in the name of the Department under the certificate of the Director of Revenue. If reproduced copies of the Department's records are offered as proof of such determination, the Director must certify that those copies are true and exact copies of records on file with the Department.

Section 5 principally addresses the burden of proof going forward in sales tax cases where no returns are filed and the methodology for the Department to provide the proper foundation for the assessment, at least as an initial matter, at a hearing or trial. Not surprisingly, and following the general rule for tax matters, an assessment in those types of cases is considered to be *prima facie* correct. While Section 5 does not particularly address the admissibility of evidence which can be used to generate an assessment, it does provide that the Department may "...use its best judgment and information" in determining the tax due and owing. Section 5 does not, by itself, limit the type of evidence the Department can rely on. Its expansive language allows the Department to use and then offer at trial the evidence which supports the assessment.

Once the Department has made its determination of tax which is presumed correct, the taxpayer may test that presumption. "If the method employed by the Department is called into question, the record must show that the techniques and assumptions which the Department used met some minimum standard of reasonableness." *Estate of Graham v. Dep't of Revenue*, 162 Ill. App. 3d 754,758 (5th Dist. 1987) (citing *Smith v. Dep't of Revenue*, 143 Ill. App. 3d 607,611 (5th Dist. 1986)). "Once the Department establishes its *prima facie* case, the burden is on the taxpayer to overcome the presumption of validity by producing competent evidence, identified by the taxpayer's books and records to show that the Department's returns are incorrect." *Smith*, 143 Ill. App. 3d at 612.

Pursuant to Section 5, the Department's tax assessments in this matter and the underlying evidence to support those assessments will be admissible at O&S' final hearing as an initial matter. O&S will be able to question the reasonableness of the Department's methodology as well as present evidence in its own books and records to rebut the presumption that the tax assessment in this matter is correct.⁶

⁶ The Department further cites to Section 8 of ROTA to support its claim that the Indiana records are admissible, but that section provides rules for the introduction of evidence in "...hearings not

The Illinois Department of Revenue also argues in its response that the Indiana Department of Revenue records are properly admissible under the Illinois Administrative Procedures Act found at 5 ILCS 100/10-5, *et seq.* Section 10-40(a) of the Act provides:

Sec. 10-40. Rules of evidence; official notice. In contested cases:

(a) Irrelevant, immaterial, or unduly repetitious evidence shall be excluded. The rules of evidence and privilege as applied in civil cases in the circuit courts of this State shall be followed. Evidence not admissible under those rules of evidence may be admitted, however, (except where precluded by statute) if it is of a type commonly relied upon by reasonably prudent men in the conduct of their affairs. Objections to evidentiary offers may be made and shall be noted in the record. Subject to these requirements, when a hearing will be expedited and the interests of the parties will not be prejudiced, any part of the evidence may be received in written form.

In the present case, the Illinois Department of Revenue claims its auditor was able to determine that the books and records of O&S were inaccurate and unreliable when he determined no purchases from MEI were recorded in those records despite being shown a handful of purchase invoices from MEI that were in O&S's possession at the time of the audit and by reviewing the Indiana records. The Department claims it was reasonable for the auditor to rely on the Indiana Department of Revenue's records which reflected MEI sales to O&S to base his calculations of corrected OTP sales to O&S.

It is rather routine for an auditor to seek third-party records, such as the Indiana records, to confirm reported entries on a company's books and records or to reconstruct the corrected income and expenses of that business. Section 10-40 of the Illinois Administrative Procedures Act, which is applicable to proceedings before the Tax Tribunal, *See* 5 ILCS 100/1-5, provides an additional basis to allow the admission of the Indiana Department of Revenue records into evidence at O&S's final hearing.

otherwise delegated to the Illinois Independent Tax Tribunal.” Section 8 of ROTA is inapplicable to this case.

Conclusion

For the foregoing reasons, the records of the Indiana Department of Revenue, which are marked for identification as Department Exhibit 2, will be admitted at O&S's final hearing before the Tax Tribunal. The remaining Department Exhibits will be admitted as well, including those portions which refer to, rely on, or are derivative of the Indiana Department of Revenue records. This ruling applies only to the admissibility and not the weight that should be afforded to those exhibits by the Tax Tribunal.

s/ James Conway
JAMES M. CONWAY
Chief Administrative
Law Judge

Date: June 30, 2016