

ILLINOIS INDEPENDENT TAX TRIBUNAL

JOHN E. ROGERS and FRANCES L. ROGERS)	
)	
Petitioner,)	
v.)	No. 14 TT 153
)	
ILLINOIS DEPARTMENT OF REVENUE)	Judge Brian F. Barov
)	
Respondent.)	

**DEPARTMENT’S REPLY IN SUPPORT OF
DEPARTMENT’S MOTION FOR SUMMARY JUDGMENT**

The Illinois Department of Revenue, (the “Department”) by and through Lisa Madigan, Attorney General of and for the State of Illinois, hereby submits its Reply brief in support of its Motion for Summary Judgment.

I. INTRODUCTION

The only issues in this case are whether the IRS assessment is “agreed to or finally determined for federal tax purposes,” and, if so, whether the Department’s Notice of Deficiency correctly determines the amount of Illinois income tax, penalty and interest resulting from that IRS assessment.

II. ARGUMENT

Section 506 of the Illinois Income Tax Act (“IITA”) requires a taxpayer to notify the Department by filing an amended return within 120 days after a federal change “is agreed to or finally determined for federal income tax purposes” 35 ILCS 5/506(b). When a taxpayer fails to timely report a federal change, the Department may issue a Notice of Deficiency at any time. 35 ILCS 5/905(d). This Tribunal must determine whether the undisputed facts show that Petitioner’s IRS assessment for the tax year ending December 31, 2002 was either “agreed to” or “finally determined” prior to the issuance of the Notice of Deficiency. 35 ILCS 5/506(b).

Taxpayer does not challenge the facts as alleged in Department's Motion for Summary Judgment. Instead, Taxpayer challenges the legal sufficiency of those facts as applied to federal law. Taxpayer argues that the IRS assessment of Taxpayer's 2002 federal adjusted gross income is incorrect, and therefore, cannot be final. The Department disagrees. However, even if the IRS assessment is wrong, the assessment is still final. Additionally, Taxpayer does not challenge the correctness of the Department's Notice of Deficiency. Finality (or finality through agreement) is the only disputed issue in this case.

- a. Federal law provides that Petitioner, as an indirect partner of Wacker Madison, is bound by the terms of the settlement agreement (Form 870-LT) entered into between Abingdon Trading and the IRS regarding the partnership items of Wacker Madison.**

Taxpayer argues in its response to Department's Motion for Summary Judgment that "the department assumes that when Abingdon (not petitioner husband as an individual) agreed to a Wacker Madison settlement that petitioner husband agreed to an amount of petitioners' 2002 adjusted gross income which is not stated or referred to in the 2008 Wacker Madison settlement." The Department assumes nothing. The Department relies on Internal Revenue Code Section 6224 (26 U.S.C. 6224), which expressly provides:

A settlement agreement between the Secretary or the Attorney General (or his delegate) and 1 or more partners in a partnership with respect to the determination of partnership items for any partnership taxable year shall (except as otherwise provided in such agreement) be binding on all parties to such agreement with respect to the determination of partnership items for such partnership taxable year. An indirect partner is bound by any such agreement entered into by the pass-thru partner unless the indirect partner has been identified as provided in section 6223 (c)(3).

26 U.S.C. 6224(c)(1) (Emphasis added). Petitioner is an indirect partner of Wacker Madison (see Department's MSJ Memorandum of Law, page 7). 26 U.S.C. § 6231(a)(10). Therefore, Petitioner is bound by the Form 870-LT entered into between Abingdon Trading and the IRS on June 19, 2008. 26 U.S.C. 6224(c). Taxpayer cites nothing for his legal argument that he is not bound as an individual taxpayer by the executed Form 870-LT.

b. The federal account transcript is a record of a government agency and therefore meets the exception to the hearsay rule in Illinois Rules of Evidence rule 803(8).

Taxpayer asserts in its response that the Federal Account Transcript (Department exhibit 2) is hearsay. Petitioner's response, Pages 7 and 8. As a general rule, any objections to exhibits should be raised by Motion. Ill. R. Evid. 103(a)(1). However, should Taxpayer raise, by motion, an objection to the Federal account transcript, Rule 803 of the Illinois Rules of Evidence provides for the admissibility of the federal account transcript. Illinois Rule of Evidence 803 provides certain exceptions to the general rule that hearsay is not admissible in evidence. Ill. R. Evid. 803. Illinois Rule of Evidence 803(8) states:

(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.

Ill. R. Evid. 803. Here, the Federal Account Transcript is a record of the activities of the IRS concerning Taxpayer's 2002 income tax account and Form U.S. 1040. Ill. R. Evid. 803(8)(A). It is also a record of activities undertaken pursuant to the agency's duty to enforce the Internal Revenue Code. Ill. R. Evid. 803(8)(B); 26 U.S.C. § 6201; 26 U.S. Code § 7801. Because the

Federal Account Transcript meets the exception to hearsay in Rule 803, it is admissible in evidence. Ill. R. Evid. 803.

c. It is irrelevant whether a bad debt deduction could be claimed by Petitioner.

Petitioner next argues that, as a result of the Wacker Madison partnership adjustment, Petitioner “would be” entitled to a bad debt deduction as the result of an uncollectible receivable from Abingdon Trading. Petitioner’s response, Page 8. This argument goes to the correctness of the IRS assessment, not the finality of it. Additionally, if such a deduction is available to Petitioner, he should file a U.S. amended return (Form 1040-X) for 2002 to claim the deduction.

d. It is irrelevant whether Taxpayer actually received a partnership distribution from Abingdon Trading to cover the Wacker Madison partnership item adjustment agreed to by Abingdon that flowed to Taxpayer’s individual income tax account.

Taxpayer argues next that the IRS and the Department are taxing Petitioner on the Wacker Madison partnership adjustment flow-through income even though Petitioner did not receive a cash distribution from Abingdon. Petitioner’s response, Pages 7 and 8. As Petitioner points out on page 11 of its brief, a partnership is an entity that files an information return showing the partnership’s income. 26 U.S.C. § 6031(a). However, that income is reported by the individual partners and taxed at the partner level. 26 U.S.C. § 701; 26 U.S.C. § 6222(a). A partnership is not required to distribute income to the partners, unless the partnership agreement requires it. And therefore, a partnership distribution is not taken into account in determining the partner’s distributive share of partnership income or loss. 26 U.S. Code § 702; *See* IRS Publication 541, “Partnership Distributions” available at:

http://www.irs.gov/publications/p541/ar02.html# en_US_201312_publink1000104228 (last visited January 9, 2015) (“A partnership distribution is not taken into account in determining the

partner's distributive share of partnership income or loss.”). Thus, the Wacker Madison partnership item adjustment (income) flows (through Abindgon Trading partnership) to Petitioner’s individual income tax return where Petitioner (partner) must pay the tax associated with that item of income. Whether Petitioner actually received the cash distribution is irrelevant.

e. Taxpayer has an Illinois remedy should the IRS reduce Taxpayer’s 2002 AGI at some future time.

The Illinois Income Tax Act provides that a Taxpayer has two years and 120 days to file a claim for refund of Illinois income tax resulting from a federal change. 35 ILCS 5/506(b); 911(b). Thus, even if the IRS reduces Taxpayer’s 2002 AGI at some time in the future as a result of Taxpayer’s various appeals or collection due process hearing, Taxpayer will have the opportunity to file an amended Illinois income tax return to reduce Taxpayer’s 2002 Illinois income tax. If Taxpayer’s AGI is decreased, as Taxpayer suggests it will be, Taxpayer will have two years and 120 days from the time the federal change becomes final to file an amended Illinois income tax return requesting a refund of overpayment of Illinois income tax. 35 ILCS 5/506(b); 911(b). Or, in the event the IRS increases Taxpayer’s 2002 AGI, Taxpayer has 120 days to file an amended return and pay any additional tax liability. 35 ILCS5/506(b).

III. CONCLUSION

The Department issued a Notice of Deficiency to Taxpayer on June 9, 2014, for the Tax year ending December 31, 2002, for underpayment of Illinois income tax resulting from a federal change. A copy of the Notice is attached as Exhibit 1 to Department’s Motion for Summary Judgment. Section 506 of the Illinois Income Tax Act (“IITA”) requires a taxpayer to notify the Department by filing an amended return within 120 days after a federal change¹ “is agreed to or

¹ A “federal change” occurs when “ the taxable income, any item of income or deduction, the income tax liability, or any tax credit reported in an original or amended federal income tax return of that person for any year or as

finally determined for federal income tax purposes” 35 ILCS 5/506(b). Department has no record of receiving a Form IL-1040-X for Taxpayer for tax year ending December 31, 2002. See Exhibit 1. As a matter of law, Taxpayer’s 2002 Adjusted Gross Income was “agreed to” on June 19, 2008, when John E. Rogers executed the Form 870-LT on behalf of Abingdon Trading, LLC. 26 U.S.C. 6224(c). Additionally, Taxpayer’s 2002 Adjusted Gross Income was “finally determined” by the IRS on May 25, 2011, when Taxpayer’s account transcript was adjusted. Nestor v. C.I.R., 118 T.C. 162, 169 (2002); Perez v. C.I.R., T.C. Memo. 2002-274, WL 31427309 (2002). Because Taxpayer failed to timely report this federal change, the Department may issue a Notice of Deficiency at any time. 35 ILCS 5/905(d). For these reasons this Tribunal should hold that the IRS assessment of Petitioner’s 2002 federal adjusted gross income was final prior to the issuance of the Notice of Deficiency and that the Notice of Deficiency correctly determined Taxpayer’s 2002 Illinois income tax. The Department respectfully requests this Tribunal order summary judgment in favor of the Department and against the Petitioner on all issues in this matter.

Respectfully submitted,

Illinois Department of Revenue
By: LISA MADIGAN, Attorney General, State of Illinois

By: _____
Jennifer Kieffer
Special Assistant Attorney General

Date: January 20, 2015

Jennifer Kieffer

determined by the Internal Revenue Service or the courts is altered by amendment of such return or as a result of any other recomputation or redetermination of federal taxable income or loss, and such alteration reflects a change or settlement with respect to any item or items, affecting the computation of such person's net income, net loss, or of any credit provided by Article 2 of this Act for any year under this Act, or in the number of personal exemptions allowable to such person under Section 151 of the Internal Revenue Code” 35 ILCS 5/506(b)(1).

Special Assistant Attorney General
Phone: (312) 814-1533
Jennifer.Kieffer@Illinois.gov

Rebecca L. Kulekowskis
Special Assistant Attorney General
Phone: (312) 814-3318
Rebecca.Kulekowskis@illinois.gov

Illinois Department of Revenue
100 West Randolph St., 7-900
Chicago, IL 60601
Fax: (312) 814-4344