ILLINOIS INDEPENDENT TAX TRIBUNAL
CHICAGO, ILLINOIS

	)	
	)	**Docket No.: 16-TT-35**
Vidicon, LLC	)	
Petitioner	)	
vs.	)	
	)	**Brian Barov**
Illinois Department of Revenue,	)	**Administrative Law Judge**
Respondent	)	

CERTIFICATE OF SERVICE BY ELECTRONIC TRANSMISION AND NOTICE OF FILING

To: (312) 606-3210
Mr. David Hughes
Horwood, Marcus and Berk
500 West Madison Street, Suite3700
Chicago, Illinois 60661

PLEASE TAKE NOTICE that on March 17, 2016, the Illinois Department of Revenue's Answer to Taxpayer's Petition was filed with the Illinois Independent Tax Tribunal by email at ITT.TaxTribunal@Illinois.gov . A copy of the attached Answer was also served on the Taxpayer's counsel listed above by email at dhughes@hmblaw.com

Respectfully submitted,

/Ronald Forman/
Ronald Forman
Special Assistant Attorney General

March 17, 2016

Ronald Forman
Special Assistant Attorney General
100 West Randolph Street, 7th Floor
Chicago, IL. 60601
(312) 814-9500

ILLINOIS INDEPENDENT TAX TRIBUNAL
CHICAGO, ILLLINOIS

VIDICON, LLC	)	
v.	)	**16-TT-35**
	)	
ILLINOIS DEPARTMENT OF REVENUE,	)	
Department	)	

ANSWER

NOW COMES the Department of Revenue of the State of Illinois ("Department"), through its attorney, Ronald Forman, Special Assistant Attorney General, and for its Answer to Taxpayer's Petition respectfully pleads as follows:

PARTIES

1. Petitioner is an Illinois limited liability company treated as a partnership for federal and state income tax purposes. Petitioner's principal business address is 300 Harvestore Dr., Dekalb, Illinois 60115.

ANSWER: The Department admits the statements contained in Paragraph 1.

2. Petitioner is represented by David A. Hughes and Christopher Lutz of Horwood Marcus & Berk Chartered, located at 500 West Madison St., Suite 3700, Chicago, Illinois 60661, who can be reached at 312-606-3212 or dhughes@hmblaw, or 312-606-3222 or clutz@hmblaw.com.

ANSWER: The Department admits the statements contained in Paragraph 2.

3. Petitioner's FEIN is 36-4413876.

ANSWER: The Department admits the statement contained in Paragraph 3.

4. The Department is an agency of the Executive Department of the State Government and is tasked with the enforcement and administration of Illinois tax laws. 20 ILCS 5/5-15.

ANSWER: The Department admits the statement contained in Paragraph 4.

NOTICE

5. On December 23, 2015, Petitioner received two Notices of Deficiency for the amount of $8,920.15 for the Tax Year ending December 31, 2010 and $658,028.43 for the Tax Year Ending December 31, 2011. True and accurate copies of the Notices of Deficiency ("Notices") are attached hereto as Exhibit A.

ANSWER: The Department admits the statements contained in Paragraph 5.

JURISDICTION

6. Petitioner brings this action pursuant to the Illinois Independent Tax Tribunal Act ("Tribunal Act"), 35 ILCS 1010/1-1 to 35 ILCS 1010/1-100.

ANSWER: The Department admits the statement contained in Paragraph 6.

7. The Tribunal has jurisdiction over this matter pursuant to sections 1-45, and 1-50 of the Tribunal Act because Petitioner timely filed this petition within 60 days of the Notices.

ANSWER: The Department admits the statement contained in Paragraph 7.

BACKGROUND

8. During the relevant tax years, Petitioner manufactured and rented light-emitting diode ("LED") video screens and related equipment for concerts and other events.

ANSWER: The Department lacks sufficient knowledge or information to form a belief as to the truth or falsity of the statement contained in Paragraph 8.

9. Petitioner's former owners, Robert J. Brigham, Jr. and Ronald Proesel, started the business in approximately January 2001.

ANSWER: The Department lacks sufficient knowledge or information to form a belief as to the truth or falsity of the statement contained in Paragraph 9.

10. Initially, Petitioner had a single customer, Nocturne Productions, Inc. ("Nocturne"), a company in the concert production business.

ANSWER: The Department lacks sufficient knowledge or information to form a belief as to the truth or falsity of the statements contained in Paragraph 10.

11. Mr. Brigham served as the COO and part owner of Nocturne but Mr. Proesel was not employed by Nocturne.

ANSWER: The Department lacks sufficient knowledge or information to form a belief as to the truth or falsity of the statements contained in Paragraph 11.

12. Petitioner initially did not manufacture the LED screens but instead purchased them from a third party.

ANSWER: The Department lacks sufficient knowledge or information to form a belief as to the truth or falsity of the statements contained in Paragraph 12.

13. Petitioner rented the LED screens and other equipment to Nocturne and Nocturne employees handled and assembled the LED screens at events.

ANSWER: The Department lacks sufficient knowledge or information to form a belief as to the truth or falsity of the statements contained in Paragraph 13.

14. In 2005, Petitioner began manufacturing the LED screens.

ANSWER: The Department lacks sufficient knowledge or information to form a belief as to the truth or falsity of the statements contained in Paragraph 14.

15. Petitioner did not have any employees in 2005 as Messrs. Brigham and Proesel were owners but not employees.

ANSWER: The Department lacks sufficient knowledge or information to form a belief as to the truth or falsity of the statement contained in Paragraph 15.

16. No other domestic company built, distributed or assembled video screens comparable to Petitioner's.

ANSWER: The Department lacks sufficient knowledge or information to form a belief as the truth or falsity of the statement contained on Paragraph 16.

17. Comparable products were available from foreign suppliers, but they were not as durable or as easy to assemble.

ANSWER: The Department lacks sufficient knowledge or information to form a belief as to the truth or falsity of the statements contained in Paragraph 17.

18. Mr. Proesel is proficient in mechanical design, has a degree in electrical engineering technology, and his expertise is in electronics.

ANSWER: The Department lacks sufficient knowledge or information to form a belief as to the truth or falsity of the statements contained in Paragraph 18.

19. Mr. Proesel was responsible for developing Petitioner's LED screens, repairing any damaged LED screens, and for assisting Nocturne employees in prepping the screens for a concert.

ANSWER: The Department lacks sufficient knowledge or information to form a belief as to the truth or falsity of the statements contained in Paragraph 19.

20. Mr. Brigham's background is in the music industry where he has extensive relationships with managers and musicians in the industry, including Herbie Herbert, a former manager for the group Journey.

ANSWER: The Department lacks sufficient knowledge or information to form a belief as to the truth or falsity of the statements contained in Paragraph 20.

21. Mr. Brigham was responsible for renting Petitioner's LED screens to customers.

ANSWER: The Department lacks sufficient knowledge or information to form a belief as to the truth or falsity of the statement contained in Paragraph 21.

22. Mr. Proesel's technical expertise coupled with Mr. Brigham's relationships turned Petitioner into the leading LED screen developer and distributor in the music industry.

ANSWER: The Department lacks sufficient knowledge or information to form a belief as to the truth or falsity of the statement contained in Paragraph 22.

23. In February 2011, Messrs. Brigham and Proesel were approached by PRG Nocturne Productions, Inc., a company that produced video screens for auto shows and theater, but not music concerts.

ANSWER: The Department lacks sufficient knowledge or information to form a belief as to the truth or falsity of the statement contained in Paragraph 23.

24. After a brief negotiation, on May 31, 2011, Petitioner sold its assets in an installment sale to PRG Nocturne Productions, Inc. for up to $70,000,000 pursuant to an Asset Purchase Agreement ("Agreement").

ANSWER: The Department lacks sufficient knowledge or information to form a belief as to the truth or falsity of the statements contained in Paragraph 24.

25. The assets sold by Petitioner included equipment, inventory, and goodwill.

ANSWER: The Department lacks sufficient knowledge or information to form a belief as to the truth or falsity of the statement contained in Paragraph 25.

26. A significant amount of the goodwill sold by Petitioner was associated with the continued employment, under the Agreement, of Messrs. Ronald Proesel and Robert Brigham, Jr.

ANSWER: The Department lacks sufficient knowledge or information to form a belief as to the truth or falsity of the statement contained in Paragraph 26.

27. PRG Nocturne Productions, Inc. understood the vital role that Messrs. Brigham and Proesel played in developing and leading Petitioner.

ANSWER: The Department lacks sufficient knowledge or belief as to the truth or falsity of the statement contained in Paragraph 27.

28. For this reason, Mr. Proesel agreed to a five year contract as co-president of PRG Nocturne Productions, Inc., and to an additional 18 month non-compete agreement, attached hereto as Exhibit B.

ANSWER: The Department lacks sufficient knowledge or information to form a belief as to the truth or falsity of the statements contained in Paragraph 28.

29. Mr. Brigham agreed to a five year contract as co-president of PRG Nocturne Productions, Inc., and to an additional 18 month non-compete agreement, attached hereto as Exhibit C.

ANSWER: The Department lacks sufficient knowledge or information to form a belief as to the truth or falsity of the statements contained in Paragraph 29.

30. PRG Nocturne Productions, Inc. purchased life insurance policies for Messrs. Proesel and Brigham.

ANSWER: The Department lacks sufficient knowledge or information to form a belief as to the truth or falsity of the statement contained in Pargarph 30.

31. In addition, PRG Nocturne Productions, Inc.'s chairman requested Messrs. Proesel and Brigham remain with the company after the initial five year employment contracts expire.

ANSWER: The Department lacks sufficient knowledge or information to form a belief as to the truth or falsity of the statements contained in Paragraph 31.

32. Messrs. Proesel and Brigham remain salaried employees of PRG Nocturne Productions, Inc. and their responsibilities include assisting in sales and management of video productions for concert tours at a national and international level, growing revenues, improving earnings, servicing customers, ensuring compliance, and managing the operations team.

ANSWER: The Department lacks sufficient knowledge or information to form a belief as to the truth or falsity of the statements contained in Paragraph 32.

33. Without the continued employment of Messrs. Proesel and Brigham, the sale price under the Agreement would have been significantly smaller.

ANSWER: The Department lacks sufficient knowledge or information to form a belief as to the truth or falsity of the statement contained in Paragraph 33.

34. Messrs. Proesel and Brigham typically earned enough in a given year that their compensation would have been similar over the seven years they committed to work for PRG Nocturne Productions, Inc. had they not sold the business.

ANSWER: The Department lacks sufficient knowledge or information to form a belief as to the truth or falsity of the statements contained in Paragraph 34.

35. Messrs. Brigham and Mr. Proesel's income as PRG Nocturne Productions, Inc. employees was significantly less than their annual distributions as the former owners of Petitioner.

ANSWER: The Department lacks sufficient knowledge or information as to form a belief as to the truth or falsity of the statements contained in Paragraph 35.

36. Upon the sale of its assets, Petitioner distributed the proceeds to its owners, Messrs. Proesel and Brigham.

ANSWER: The Department lacks sufficient knowledge or information to form a belief as to the truth or falsity of the statement contained in Paragraph 36.

37. In distributing the sale proceeds to its owners, Petitioner deducted the payments made to Messrs. Proesel and Brigham as compensation for services rendered by partners of the partnership.

ANSWER: The Department lacks sufficient knowledge or information to form a belief as to the truth or falsity of the statement contained in Paragraph 37.

38. Messrs. Proesel and Brigham reported the sale proceeds on their individual Illinois income tax returns and paid Illinois income tax on those proceeds.

ANSWER: The Department lacks sufficient knowledge or information to form a belief as to the truth or falsity of the statement contained in Paragraph 38.

39. On audit, the Department determined that Petitioner was not entitled to deduct the payments made to Messrs. Proesel and Brigham.

ANSWER: The Department admits that a portion of the deduction taken for personal service income on the Taxpayer's 2010 and 2011 tax returns was disallowed. The

adjustments are reflected on the Department's Notices attached to the Taxpayer's Petition in Exhibit A.

40. The Department issued the Notices reflecting tax on the income that was deducted as compensation for services rendered by the partners.

ANSWER: The Department denies the statement contained in Paragraph 40.

COUNT I

Petitioner is Entitled to A Deduction for the Compensation Paid to its Partners for Services Rendered

41. Petitioner realleges and incorporates by this reference the allegations made in paragraphs 1 through 40, inclusive, hereinabove.

ANSWER: The Department incorporates and repeats its answers to Paragraphs 1 through 40.

42. The Illinois Income Tax Act allows a partnership to deduct "[a]ny income of the partnership which constitutes personal service income as defined in Section 1348(b)(1) of the Internal Revenue Code (as in effect December 31, 1981) or a reasonable allowance for compensation paid or accrued for services rendered by partners to the partnership, whichever is greater." 35 ILCS 5/203(d)(2)(H).

ANSWER: Paragraph 42 contains a legal conclusion, not a material allegation of fact, and therefore, does not require an answer pursuant to Rule 310(b)(2). The statute speaks for itself.

43. Internal Revenue Code Section 1348, as in effect on December 31, 1981, provided that "personal service income" consists of "[a]ny income which is earned income

within the meaning of section 401(c)(2)(C) or section 911(b) or which is an amount received as a pension or annuity which arises from an employer-employee relationship or from tax deductible contributions to a retirement plan."

ANSWER: Paragraph 43 contains a legal conclusion, not a material allegation of fact, and therefore, does not require an answer pursuant to Rule 310(b0(2).

44. Internal Revenue Code section 911(b), as in effect on December 31, 1981, provided that the term "earned income" means wages, salaries, or professional fees, and other amounts received as compensation for personal services actually rendered, but does not include that part of compensation derived by the taxpayer for personal profits rather than a reasonable allowance as compensation for services actually rendered.

ANSWER: Paragraph 44 contains a legal conclusion, not a material allegation of fact, and therefore, does not require an answer pursuant to Rule 310(b)(2).

45. Although the Agreement states that a significant portion of the sale was attributable to goodwill, the Agreement contains no definition of the term "goodwill," nor does it provide any schedules or explanation as to the value of the goodwill.

ANSWER: The Department lacks sufficient knowledge or information to form a belief as to the truth or falsity of the statements contained in Paragraph 45.

46. A significant amount of the value of Petitioner is derived from the personal efforts, abilities, and services of Messrs. Proesel and Brigham.

ANSWER: The Department denies the statements contained in Paragraph 46.

47. A significant portion of the gain was directly attributable to the continued employment and non-compete agreements of Messrs. Proesel and Brigham.

ANSWER: The Department denies the statement contained in Paragraph 47.

48. The value of Petitioner's assets was generated largely by the personal efforts of Messrs. Proesel and Brigham.

ANSWER: The Department lacks knowledge or information to form a belief as to the truth or falsity of the statement contained in Paragraph 48.

49. Because the personal efforts of Messrs. Proesel and Brigham created the value of the assets that were sold to PRG Nocturne Productions, Inc., Petitioner was entitled to deduct as compensation paid for personal services rendered by its partners the gain on the sale.

ANSWER: The Department denies the statements contained in Paragraph 49

WHEREFORE, the Department prays that the Tribunal enter an order that:

(a) Denies each prayer for relief in Count I of the Taxpayer's Petition;

(b) Finds the Notices of Deficiency are correct;

(c) Orders judgement in favor of the Department and against the Taxpayer; and

(d) Grants any relief this Tribunal deems just and appropriate.

COUNT II

<u>All penalties should be abated based on reasonable cause</u>

50. Petitioner realleges and reincorporates the allegations in paragraphs 1 through 49, inclusive, hereinabove.

ANSWER: The Department incorporates and repeats its answers to paragraphs 1 through 49.

51. In its Notices, Defendants assessed penalties in an amount totaling $81,269.10.

ANSWER: The Department admits the statement contained in Paragraph 51.

52. Illinois law provides that penalties do not apply if a taxpayer shows that its failure to pay tax at the required time was due to reasonable cause. 35 ILCS §734-8.

ANSWER: Paragraph 52 contains a legal conclusion, not an allegation of material fact, and therefore, does not require an answer pursuant to Rule 310(b)(2). The statute in its entirety speaks for itself.

53. 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 its proper tax liability and to pay its proper tax liability in a timely fashion. 86 Ill. Admin. Code §700.400(b).

ANSWER: Paragraph 53 contains a legal conclusion, not an allegation of material fact, and therefore, does not require an answer pursuant to Rule 310(b)(2). The regulation in its entirety speak for itself.

54. A taxpayer will be considered to have made a good faith effort to determine and pay its proper tax liability if it exercised ordinary business care and prudence in doing so. 86 Ill. Admin. Code §700.400(b).

ANSWER: Paragraph 54 contains a legal conclusion, not an allegation of material fact, and therefore, does not require an answer pursuant to Rule 310(b)(2). The regulation in its entirety speaks for itself.

55. Petitioner reasonably deducted the receipts from its income that it paid to its partners for services rendered.

ANSWER: The Department denies the statement contained in Paragraph 55.

56. Petitioner, relying on Illinois law and regulations, exercised ordinary business care and prudence when it reasonably determined its Illinois income tax liability.

ANSWER: The Department denies the statements contained in Paragraph 56.

57. The Department's determination that Petitioner owes penalties on late payment of tax is not supported by fact or law.

ANSWER: The Department denies the statements contained in Paragraph 57.

WHEREFORE, the Department prays that the Tribunal enter an order that:

(a) Denies each prayer for relief in Count II of the Taxpayer's Petition;

(b) Finds the Notices of Deficiency are correct;

(c) Orders judgement in favor of the Department and against the Taxpayer; and

(d) Grants any further relief this Tribunal deems just and appropriate.

Respectfully Submitted,

LISA MADIGAN
Attorney General
State of Illinois

By: /Ronald Forman/_____
Ronald Forman
Special Assistant Attorney General

Ronald Forman
Special Assistant Attorney General
Illinois Department of Revenue
Office of Legal Services
100 W. Randolph St., 7-900
Chicago, IL 60601
Telephone: (312) 814-9500
Email: ronald.forman@illinois.gov

STATE OF ILLINOIS)
) SS
COUNTY OF COOK)

VIDICON, LLC
v.

ILLINOIS DEPARTMENT OF REVENUE

DOCKET NO. 16-TT-35

VERIFICATION AND AFFIDAVIT AS TO LACK OF SUFFICIENT KNOWLEDGE

Julia Brown, being first duly sworn, deposes and says that she is an employee and duly authorized agent of the Illinois Department of Revenue ("Department"), that she has read the foregoing Department's Answers to Taxpayer's Petition, that she is well acquainted with its contents, and under penalties as provided by law pursuant to 735 ILCS 5/1-109 of the Illinois Code of Civil Procedure, she certifies that the statements set forth in that instrument are true and correct, except as to allegations claiming lack of sufficient knowledge (Paragraphs 8-38, 45 and 48) pursuant to 735 ILCS 5/2-610(b), which she verily believes to be true.

Julia Brown

Julia Brown
Revenue Auditor
Illinois Department of Revenue