

ILLINOIS INDEPENDENT
TAX TRIBUNAL

INTERNATIONAL BUSINESS MACHINES
CORPORATION,

Petitioner.

v.

ILLINOIS DEPARTMENT OF REVENUE,

Respondent.

Case No. 16 T 115



Petitioner, International Business Machines Corporation, by and through its attorneys, Sutherland Asbill & Brennan LLP, hereby petitions the Illinois Independent Tax Tribunal to review and reverse the Notices of Deficiency (“Notices”) issued by the Illinois Department of Revenue, for the reasons stated below:

PARTIES

1. Petitioner, International Business Machines Corporation (“IBM”), is a publicly traded corporation duly organized and existing under the laws of New York.
2. Petitioner maintains its principal place of business at 1 New Orchard Road, Armonk, New York 10504-1722.
3. Petitioner’s telephone number is (914) 499-1900.
4. Petitioner’s tax identification number is 13-0871985.
5. Petitioner is represented by Sutherland Asbill & Brennan LLP attorney Marc A. Simonetti, who is located at The Grace Building, 40th Floor, 1114 Avenue of the Americas, New York, NY 10036-7703 and can be reached at (212) 389-5015 or

marc.simonetti@sutherland.com.

6. Respondent, Illinois Department of Revenue (“Department”), is an agency of the state of Illinois responsible for administering and enforcing the revenue laws of the state of Illinois.

JURISDICTION

7. On March 31, 2016, the Department issued the Notices to IBM assessing a total balance due of \$19,159,241.00 in tax; \$3,831,848.20 in penalty; and \$2,791,586.68 in interest for the tax years ended December 31, 2009 and December 31, 2010. The Notice of Deficiency for the tax year ended December 31, 2009 asserts a total tax deficiency of \$9,737,283. The Notice of Deficiency for the tax year ended December 31, 2010 asserts a total tax deficiency of \$9,421,958. A copy of the Notices is attached as **Exhibit A**.
8. This Tribunal has original jurisdiction over all Department determinations reflected in Notices of Deficiency where the amount at issue exceeds \$15,000.00, exclusive of penalties and interest. 35 Ill. Comp. Stat. 1010/1-45.

BACKGROUND

9. IBM World Trade Corporation (“WTC”) is a Delaware corporation with its headquarters in New York.
10. WTC is a wholly-owned subsidiary of IBM.
11. In 1949, IBM contributed its foreign assets and foreign securities to WTC.
12. During the audit period, WTC conducted its business operations primarily outside the United States.

13. WTC did not make any sales in the U.S.
14. Historically, WTC licensed from IBM the right to sublicense computer hardware technology and software technology in foreign countries.
15. IBM and WTC established the terms of the Hardware Royalty agreement in 1963.
16. IBM and WTC established the terms of the Software License agreement in 1988.
17. IBM and WTC entered into three Cost Sharing Agreements, one each for hardware, software, and services (collectively, the “CSA”), effective January 1, 2007.
18. IBM is the legal owner of the intellectual property behind its hardware and software technology, while WTC is the beneficial owner for the geographic territories assigned to it under the CSA.
19. Pursuant to the CSA, WTC shares research and development costs (“R&D”) and selling, general, and administrative expenses (“SG&A”) with IBM.
20. WTC receives royalties from the controlled foreign corporations (“CFCs”) related to the sale of hardware, software, and services.
21. WTC also sells directly to third party customers outside the U.S.
22. License agreements have been periodically amended to adjust the hardware royalty rates and software royalty rates according to updated transfer pricing studies.
23. The most recent software royalty transfer pricing study indicated that the royalty is within the interquartile range for comparable uncontrolled software license transactions.
24. In 2009, WTC had seventeen employees in the United States, all based in New York.
25. In 2010, WTC had four employees in the United States, all based in New York.
26. In 2009 and 2010, WTC operated a network of foreign branches that employed hundreds of employees and many contractors outside the United States.

27. WTC's branch employees performed sales distribution functions, including sales, finance, human resources, marketing, sales operations, delivery, and customer service.
28. In 2009 and 2010, WTC had approximately six directors, and between nine and eleven officers, some of whom were also directors or officers of IBM.
29. Most of WTC's directors and officers were directors or officers of many other IBM subsidiaries.
30. In 2009, WTC had everywhere payroll of approximately \$17 million and U.S. payroll of approximately \$1.2 million.
31. In 2010, WTC had everywhere payroll of approximately \$17.7 million and U.S. payroll of approximately \$336,000.
32. In 2009, WTC had everywhere property of approximately \$66.7 million and U.S. property of approximately \$177,000.
33. In 2010, WTC had everywhere property of approximately \$66 million and U.S. property of approximately \$9,000.

PROCEDURAL HISTORY

34. The Department audited IBM's income tax returns for tax years ended December 31, 2009 and December 31, 2010 ("Audit Period").
35. IBM responded to all audit information requests in a timely and sufficient manner.
36. As a result of the audit, the Department issued an assessment of additional tax because the Department disregarded WTC's statutory characterization as an excluded "80/20 Company." A copy of the 80/20 calculation workpapers is attached as **Exhibit B**.

37. The Department imputed additional property and payroll to WTC for purposes of the 80/20 test.
38. The Department provided workpapers that detailed its assumptions and calculations for the 80/20 test.
39. The Department imputed property and payroll to WTC based on unverified information from websites, such as corporationwiki.com, manta.com, and hoover.com.
40. Open source websites such as corporationwiki.com allow anyone to enter or change information on the site.
41. The Department imputed property and payroll to WTC based on several faulty and baseless assumptions.
42. During the audit, IBM provided the Department with documentation illustrating that in 2009, WTC had seventeen employees in the United States, all based in New York; and that in 2010, WTC had four employees in the United States, all based in New York.
43. The Department ignored the information IBM provided and instead re-computed WTC's U.S. property fraction by calculating a rent amount determined by multiplying a fabricated number of WTC employees by a fabricated per employee rental rate.
44. The Department calculated the imputed U.S. rent based on 400 WTC U.S. employees.
45. The Department conceived the number of employees based on Internet postings on an unverified open-source website.
46. The Department conceived an assumption of 250 square feet per employee (400 square feet per officer); more than 7,000 square feet of common space; and rent at \$15 per square foot, for a total imputed U.S. rent of \$13.5 million per year.
47. The Department provided no support for its rental assumptions.

48. The Department also imputed \$1.68 million per year for U.S. capital leases (vehicles) for executives and salesmen. The Department used an assumption of \$350/month per vehicle for 50 vehicles.
49. The Department provided no support for its capital lease assumptions.
50. During the audit, IBM informed the Department that WTC did not provide any vehicles to any employees, officers, or directors.
51. The Department devised U.S. compensation for WTC officers and directors by imputing 100% of their IBM compensation to WTC.
52. These officers and directors did not work exclusively for WTC.
53. The Department ignored the official list of WTC officers and directors, and their IBM W-2 wages provided by IBM.
54. Instead, the Department grossly overestimated the officers' and directors' IBM compensation based on information from unreliable sources.
55. During the audit, IBM explained that even if the Department had the authority to impute payroll—which it does not—that the Department could not impute 100% of the officers' and directors' IBM wages to WTC.
56. The Department also imputed a portion of the IBM Chairman's compensation to WTC, even though he was not an officer, director, or employee of WTC.
57. The Department also imputed 100% of another individual's compensation to WTC, even though he was not an officer, director, or employee of WTC, based entirely on information from corporationwiki.com.
58. The Department expressly recognized that it could not impute any of IBM's payroll under the CSA to WTC.

59. The Department's workpapers stated that "IBM Corporation's Salaries claimed for R&D Tax credit are excluded from WTC 80/20 calculation."
60. During the audit, to illustrate the Department's flawed analysis, IBM provided a calculation that used the ratio of IBM's gross receipts to WTC's gross receipts as a proxy to divide the officers' and directors' wages between the two entities.
61. Even imputing wages using the gross receipts ratio, WTC still qualified as an 80/20 Company.
62. On November 21, 2014, the Department issued a Notice of Proposed Deficiency assessing an additional liability in the amount of \$19,157,894.00 in tax; and \$2,873,684.00 in penalties, for the Audit Period (the Notice of Proposed Deficiency did not calculate interest).
63. On January 16, 2015, IBM submitted a request for an Informal Conference Board review of the Notice of Proposed Deficiency pursuant to Ill. Admin. Code tit. 86, § 215.115.
64. The Informal Conference Board hearing was adjourned shortly after it began because two board members were called away from the hearing.
65. IBM requested a full hearing.
66. The Informal Conference Board denied IBM a full hearing.
67. IBM requested that the Informal Conference Board reconsider its denial and grant a full hearing so that IBM could provide any additional information (beyond the voluminous information IBM provided during the audit) that the Department might want for the 80/20 Company determination.
68. The Informal Conference Board expressly "concluded there was no additional information needed by the Informal Conference Board for its deliberation of IBM's

objections to the Notice of Proposed Deficiency.” See email from Informal Conference Board Conferee attached as **Exhibit C**.

69. On January 11, 2016, the Informal Conference Board issued an Action Decision sustaining the Department’s Notices of Proposed Deficiency.
70. On March 31, 2016, the Department issued the Notices to IBM assessing a total balance due of \$19,159,241.00 in tax; \$3,831,848.20 in penalty; and \$2,791,586.68 in interest for the tax years ended December 31, 2009 and December 31, 2010.

FIRST COUNT

The Department Does Not Have the Authority to Impute Property and Payroll for Purposes of the 80/20 Test.

71. IBM hereby restates and realleges the allegations contained in paragraphs 1 through 70 as if set forth fully herein.
72. Illinois tax law limits the composition of a unitary combined return to a water’s-edge combined filing methodology. 35 Ill. Comp. Stat. 5/1501(a)(27)(A).
73. A taxpayer must compute each unitary entity’s business activity to determine whether it is included in the Illinois water’s-edge unitary combined group return.
74. An Illinois unitary combined group does not include a unitary entity if its business activity outside the United States is 80% or more of its total business activity (commonly referred to as an 80/20 Company). *Id.*; see also *Dover Corp. v. Illinois Dep’t of Revenue*, No.98 L 50170 (Ill. Cir. Ct. Cook Jan. 14, 2000).
75. Illinois tax law expressly provides that an 80/20 Company cannot be included in the Illinois unitary combined return. 35 Ill. Comp. Stat. 5/1501(a)(27)(A).

76. Illinois Tax Law requires the comparison of United States business activity to worldwide business activity (“Business Activity Test”). 35 Ill. Comp. Stat. 5/1501(a)(27)(A); Ill. Admin. Code tit. 86, § 100.9700(c).
77. The Business Activity Test involves two fractions—property and payroll. The numerators of the fractions represent property and payroll from sources within the United States, and the denominators of the fractions represent respective worldwide property and payroll.¹ *Id.*
78. Illinois regulations provide that the fractions shall be gross figures without intercompany eliminations based on the entity’s membership in any unitary business group. Ill. Admin. Code tit. 86, § 100.9700(c).
79. The taxpayer must compute each entity’s property and payroll fractions using the same methodology for both Business Activity Test and apportionment purposes. *Id.*
80. A taxpayer must average the two fractions to arrive at its business activity fraction. *Id.*
81. The property fraction is a fraction comprised of a numerator, which is the average value of the United States real and tangible personal property owned or rented and used in the trade or business during the taxable year; and a denominator, which is the average value of all the real and tangible personal property owned or rented and used in the trade or business during the taxable year. 35 Ill. Comp. Stat. 5/304(a)(1)(A). The value of property is averaged using the beginning and end of year balances. 35 Ill. Comp. Stat. 5/304(a)(1)(C).
82. The payroll fraction is a fraction comprised of a numerator, which is the total compensation paid within the United States during the taxable year; and a denominator,

¹ Illinois tax law ultimately requires the taxpayer to subtract its business activity fraction from 1 to determine whether the taxpayer’s foreign business activity exceeds 80%.

which is the total compensation paid everywhere during the taxable year. 35 Ill. Comp. Stat. 5/304(a)(2)(A).

83. If the employer-employee relationship does not exist, any payment for services performed does not constitute “compensation.” Ill. Admin. Code tit. 86, § 100.3100(b).
84. Illinois regulations expressly provide that “employee” includes an individual performing services only if the relationship between the person and the entity for which the person performs such services is the “legal relationship of employer and employee.” *Id.*
85. The Department does not have the authority to impute property or payroll for purposes of the 80/20 Business Activity Test.
86. The Office of Administrative Hearings expressly stated that the Department is precluded from imputing payroll from one company to another when the employees in question (including directors and officers) provide only minor services or receive no compensation from the entity, when the companies have economic substance. *Ill. Dep't of Revenue v. Shanghai, Inc.*, IT 02-1 (Office of Admin. Hearings Feb. 7, 2002).
87. IBM employees, directors, and officers provide only minor services to WTC and receive no compensation from WTC.
88. WTC has hundreds of employees worldwide who conduct WTC’s business operations.
89. Because Illinois statutorily excludes 80/20 Companies from the unitary group return, the 80/20 Company’s income is necessarily excluded from the unitary group’s Illinois taxable income.

WHEREFORE, the Petitioner demands judgment as follows:

- (a) That WTC was properly considered an 80/20 Company during the Audit Period;
- (b) That the Department does not have the authority to impute property or payroll for

80/20 test purposes;

(c) That the Department's Notices of Deficiency and assessment of income tax for the Audit Period in the amount of \$19,159,241.00 and all interest and penalties thereon be vacated, reversed, and set aside in its entirety; and

(d) Such other and further relief as the Tribunal may deem just and appropriate.

SECOND COUNT

Even if the Department had Authority to Impute, the Department Improperly Imputed Additional Property and Payroll to WTC for Purposes of Calculating the Property and Payroll Fractions Under the 80/20 Test.

90. IBM hereby restates and realleges the allegations contained in paragraphs 1 through 89 as if set forth fully herein.
91. Even if the Department had the authority to impute property or payroll from one entity to another for purposes of the 80/20 test—which it does not—WTC still qualifies as an 80/20 Company when accurate data is used to calculate the adjustments.
92. Specifically, the Department has adjusted WTC's business activity fractions by imputing additional United States property and payroll to WTC.
93. Even using the Department's faulty methodology to impute additional United States presence to WTC, based on WTC's actual facts WTC continues to have more than 80% of its business activity outside the United States.

Property Fraction

94. The Department imputed additional U.S. property to WTC for purposes of calculating the property fraction.

95. During the audit, IBM provided the Department with documentation illustrating that WTC had between four and seventeen statutory employees in the U.S. during the Audit Period.
96. The Department ignored the information IBM provided and instead calculated a rent amount based on multiplying a fabricated number of WTC employees by a fabricated per employee rental rate.
97. The Department's calculation of the imputed rent is flawed because it is based on a completely inaccurate number of WTC employees.
98. The Department relied on unverifiable and inaccurate sources—such as corporationwiki.com, www.manta.com, and www.hoover.com, among others—to compute WTC's property fraction.
99. The Department calculated the imputed U.S. rent based on 400 WTC U.S. employees.
100. The Department conceived the number of employees based on Internet postings on an open-source website.
101. The Department conceived an assumption of 250 square feet per employee (400 square feet per officer); more than 7,000 square feet of common space; and rent at \$15 per square foot, for a total imputed U.S. rent of \$13.5 million per year.
102. The Department provided no support for its rental assumptions.
103. The Department also imputed \$1.68 million per year for U.S. capital leases (vehicles) for executives and salesmen. The Department used an assumption of \$350/month per vehicle for 50 vehicles.
104. During the audit, IBM informed the Department that WTC did not provide any vehicles to any employees, officers, or directors.

105. The Department provided no support for its capital lease assumptions.
106. In its workpapers, the Department miscalculated WTC's as-filed property figures, which produced inflated U.S. property figures.
107. During the Audit Period, WTC had between four and seventeen employees in the United States as defined in Illinois tax law and regulations. *See* Ill. Admin. Code tit. 86, § 100.3100(b).
108. Even using the Department's faulty rental rate and square footage guesses, using WTC's accurate number of U.S. employees yields a foreign property fraction that exceeds 97% for the Audit Period.
109. Therefore, WTC remains an 80/20 Company, even if the Department were permitted to impute additional property to it, using the Department's methodology but with the accurate number of employees.

Payroll Fraction

110. The Department also imputed additional U.S. payroll to WTC for purposes of calculating the payroll fraction.
111. The Department's calculation of the imputed payroll is flawed because it is based on completely inaccurate compensation figures and alleged number of employees.
112. The Department devised U.S. compensation for WTC officers and directors by imputing all of their IBM compensation to WTC.
113. The Department ignored the official list of WTC officers and directors, and their IBM W-2 wages that IBM provided to the Department.
114. Instead, the Department grossly overestimated the officers' and directors' IBM compensation based on information from unreliable sources.

115. The Department also imputed a portion of the IBM Chairman's compensation to WTC, even though he was not an officer, director, or employee of WTC.
116. The Department also imputed 100% of another individual's compensation to WTC, even though he was not an officer, director, or employee of WTC, based entirely on information from corporationwiki.com.
117. During the audit, IBM explained that even if the Department had the authority to impute payroll—which it does not—that the Department could not impute 100% of the officers' and directors' IBM wages to WTC.
118. During the audit, to illustrate the Department's flawed analysis, IBM provided a calculation that used the ratio of IBM's gross receipts to WTC's gross receipts as a proxy to divide the officers' and directors' wages between the two entities.
119. Even imputing wages using the gross receipts ratio, WTC had a payroll fraction that is between 78% to 86% for the Audit Period.
120. Consequently, even if the Department were permitted to impute property and payroll and the Department's methodology were correct—neither of which are true—using accurate figures, WTC had 87.9% of its business activity outside of the United States in 2009 and 92.5% in 2010.
121. Therefore, WTC is an 80/20 Company based on the express Illinois statutory requirements.
122. Because WTC is an 80/20 Company for the entire Audit Period based on the correct calculations, it was improper for WTC to be included in IBM's unitary combined return. WHEREFORE, the Petitioner demands judgment as follows:
 - (a) That WTC was properly considered an 80/20 Company during the Audit Period;

(b) That the Department does not have the authority to impute property or payroll for 80/20 test purposes;

(c) That the Department's Notices of Deficiency and assessment of income tax for the Audit Period in the amount of \$19,159,241.00 and all interest and penalties thereon be vacated, reversed, and set aside in its entirety; and

(d) Such other and further relief as the Tribunal may deem just and appropriate.

THIRD COUNT

The Department Bears—and Failed to Carry—the Burden to Prove that WTC Was Not an 80/20 Company

123. IBM hereby restates and realleges the allegations contained in paragraphs 1 through 122 as if set forth fully herein.

124. The Department bears the burden of proof because IBM offered adequate books and records to the Department for review, but the Department disregarded those books and records and instead based its assessment on unverifiable and inaccurate sources.

125. IBM provided sufficient documentation during the audit that proved that WTC was an 80/20 Company.

126. In addition, after IBM requested an Informal Conference Board hearing, IBM expressly stated that it would provide any additional documentation the Department thought necessary to illustrate that WTC was an 80/20 Company.

127. The Department refused to acknowledge the voluminous documentation IBM provided during the audit (*e.g.*, actual W-2 wage data) and expressly refused to accept any additional documentation.

128. Instead, the Department improperly asserted that WTC was not an 80/20 Company based on unverifiable and inaccurate sources of information, including open source websites such as corporationwiki.com.
129. The Department's Notice of Deficiency is not presumed to be correct, and the Department must carry the burden of proof in this proceeding because the Department's Notice of Deficiency is based on an inadequate review of the taxpayer's books and records. *See Taylor v. Helvering*, 293 U.S. 507 (1935); *United States v. Janis*, 428 U.S. 433 (1976); *see also J.H. Walters & Co. v. Dep't of Rev.*, 44 Ill.2d 95 (Ill. 1969).
130. Additionally, the Department must carry the burden of proof because IBM offered adequate books and records to the Department for review, but the Department opted to base its conclusion on unverifiable and inaccurate sources, and thus used an indirect method to calculate tax due. *See Ruth v. United States*, 823 F.2d 1091, 1094 (7th Cir. 1987); *Pittman v. Comm'r*, 100 F.3d 1308, 1313 (7th Cir. 1996); *Zuhones v. Comm'r*, 883 F.2d 1317, 1325 (7th Cir. 1989); *Mitchell v. Dep't of Revenue*, 230 Ill. App.3d 795, 800 (Ill. App. Ct. 1992); *see also Names in the News v. New York State Tax Comm'n*, 75 A.D.2d 145, 147 (N.Y. Sup. Ct. App. Div. 1980); *Matter of Chartair, Inc. v. State Tax Comm'n*, 65 A.D.2d 44 (N.Y. Sup. Ct. App. Div. 1978).
131. When a taxpayer provides evidence that "is not so inconsistent or improbable in itself as to be unworthy of belief, the burden then shifts to the Department which is required to prove its case by competent evidence." *Fillichio v. Dep't of Revenue*, 15 Ill.2d 327, 333 (Ill. 1958); *see also, PPG Industries, Inc. v. Dep't of Revenue*, 328 Ill. App.3d 16 (Ill. Ct. App. 2002); *Goldfarb v. Dep't of Revenue*, 411 Ill. 573 (Ill. 1952).

132. The Department disregarded IBM's sufficient documentation proving that WTC was an 80/20 Company.
133. Additionally, IBM offered to provide supplemental documentation further demonstrating that WTC was an 80/20 Company.
134. The Department refused to accept any supplemental documentation.
135. Instead, the Department relied on unverifiable and inaccurate sources to assert that WTC was not an 80/20 Company.
136. Consequently, the Department bears the burden to prove that WTC was not an 80/20 Company.
137. The Department failed to carry its burden to prove that WTC was not an 80/20 Company.

WHEREFORE, the Petitioner demands judgment as follows:

- (a) That the Department did not carry its burden to prove that WTC did not qualify as an 80/20 Company during the Audit Period;
- (b) That the Department's Notices of Deficiency and assessment of income tax for the Audit Period in the amount of \$19,159,241.00 and all interest and penalties thereon be vacated, reversed, and set aside in its entirety; and
- (c) Such other and further relief as the Tribunal may deem just and appropriate.

FOURTH COUNT

Penalties Must Be Abated for Reasonable Cause

138. IBM hereby restates and realleges the allegations contained in paragraphs 1 through 137 as if set forth fully herein.
139. Any penalties must be abated for reasonable cause.
140. The Department assessed penalties for the Audit Period in the amount of \$3,831,848.20.

141. Under Illinois law, no penalties shall be imposed on a taxpayer if his failure to pay tax was due to reasonable cause. 35 Ill. Comp. Stat. 735/3-8.
142. 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.” Ill. Admin. Code tit. 86, § 700.400(b).
143. A taxpayer is considered to have made a good faith effort to determine, file, and pay his tax liability if “he exercised ordinary business care and prudence in doing so.” Ill. Admin. Code tit. 86, § 700.400(c).
144. A taxpayer’s filing history is also considered when determining whether there is reasonable cause. Ill. Admin. Code tit. 86, § 700.400(d).
145. IBM followed the statutory requirements set forth in Illinois tax law to determine whether WTC was an 80/20 Company.
146. Pursuant to the statutory requirements, WTC is an 80/20 Company and IBM properly excluded WTC from its Illinois combined return.
147. The Department attempts a discretionary adjustment, which renders penalties inappropriate.
148. IBM made a good faith effort to determine its proper tax liability and to file and pay its proper tax liability in a timely fashion.
149. IBM exercised ordinary business care and prudence in determining its proper tax liability and filing and paying its proper tax liability in a timely fashion.
150. IBM has a long history of timely filing Illinois corporate income tax returns and paying Illinois corporate income tax in a timely manner.

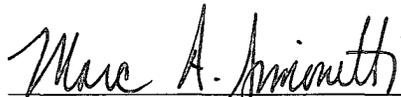
151. The penalties imposed by the Department must be abated for reasonable cause.

WHEREFORE, the Petitioner demands judgment as follows:

- (a) That all penalties assessed by the Department be abated in full; and
- (b) Such other and further relief as the Tribunal may deem just and appropriate.

SUTHERLAND ASBILL & BRENNAN LLP
Attorneys for Petitioner

By:



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DATED: May 25, 2016

EXHIBIT A

Notice of Deficiency

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



March 31, 2016



Letter ID: CNXXX15658312488

#BWNKMGV
#CNXX X156 5831 2488#

SUTHERLAND ASBILL & BRENNAN LLP

ATTN: MARC SIMONETTI RE: IBM

1114 AVENUE OF THE AMERICAS FL 40
NEW YORK NY 10036-7703

Taxpayer ID: 13-0871985
Audit ID: A488620032
Reporting period: December 2009
Total Deficiency: \$13,285,652.63
Balance due: \$13,285,652.63

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 the "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 is 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 the date 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 and administrative hearing. An administrative hearing is a formal legal proceeding conducted pursuant to the 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). 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 liability under protest using Form RR-374, Notice of Payment Under Protest (available on our website at 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 assessment total 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

cc: SUTHERLAND ASBILL & BRENNAN
1114 AVE OF THE AMERICAS 40TH FL
NEW YORK, NY 10036

Bankruptcy Information

If you are currently under the protection of the Federal Bankruptcy Court, contact us and provide the bankruptcy number and the bankruptcy court. The bankruptcy automatic stay does not change the fact you are required to file tax returns.

Taxpayer Bill of Rights

- You have the right to call the Department of Revenue for help in resolving tax problems.
- You have the right to privacy and confidentiality under most tax laws.
- You have the right to respond, within specified time periods, to Department notices by asking questions, paying the amount due, or providing proof to refute the Department's findings.
- You have the right to appeal Department decisions, in many instances, within specified time periods, by asking for Department review, by filing a petition with the Illinois Independent Tax Tribunal, or by filing a complaint in circuit court.
- If you have overpaid your taxes, you have the right, within specified time periods, to file for a credit (or, in some cases, a refund) of that overpayment.

The full text of the Taxpayers' Bill of Rights is contained in the Illinois Compiled Statutes, 20 ILCS 2520/1 et seq.

Statement

Date: March 31, 2016
Name: INTERNATIONAL BUSINESS MACHINES CORP
Taxpayer ID: 13-0871985
Letter ID: CNXXX15658312488

The attached EDA-27, Explanation of Adjustments, details your audit adjustments.

Computation of deficiency

Reporting period: 31-Dec-2009

Income or loss	
Federal taxable income	\$7,470,599,919.00
Net operating loss deduction	\$111,802,024.00
State Municipal and other interest excluded	\$7,385,397.00
Income tax and replacement tax deduction	\$4,253,675.00
Illinois bonus depreciation addition	\$1,024,030,737.00
Related party expenses additions	\$148,520,000.00
Other additions	\$0.00
Income or loss	\$8,766,591,752.00
Base income or loss	
Foreign dividends subtraction	\$3,154,794,026.00
Illinois bonus depreciation subtraction	\$553,675,386.00
Total subtractions	\$3,708,469,412.00
Base income or net loss	\$5,058,122,340.00
Income allocable to Illinois	
Non-business income or loss	\$0.00
Non-unitary partnership bus. income or loss	-\$846,634.00
Business income or loss	\$5,058,968,974.00
Apportionment formula	
Total sales everywhere	\$30,154,435,431.00
Total Illinois sales	\$1,146,751,918.00
Apportionment factor	0.038029
Business income/loss apportionable to IL	\$192,387,531.00
Nonbusiness income/loss allocable to IL	\$0.00
Non-unitary part. business income app. to IL	\$0.00
Base income or net loss allocable to IL	\$192,387,531.00
Net income	
Base income or net loss	\$192,387,531.00
IL net loss deduction (NLD)	\$0.00
Net income	\$192,387,531.00
Net replacement tax	
Replacement tax	\$4,809,688.00
Recapture of investment credits	\$0.00
Replacement tax before credits	\$4,809,688.00
Replacement tax investment credits	\$0.00
Net replacement tax	\$4,809,688.00

Statement

Date: March 31, 2016
Name: INTERNATIONAL BUSINESS MACHINES CORP
Taxpayer ID: 13-0871985
Letter ID: CNXXX15658312488

Computation of deficiency

Reporting period: 31-Dec-2009

Net income tax	
Income tax	\$9,234,601.00
Recapture of investment credits	\$0.00
Income tax before credits	\$9,234,601.00
Income tax investment credits	\$187,368.00
Net income tax	\$9,047,233.00
Refund or balance due	
Net replacement tax	\$4,809,688.00
Net income tax	\$9,047,233.00
Total net income and replacement tax due	\$13,856,921.00
Minus tax previously assessed	-\$4,119,638.00
Total tax deficiency	\$9,737,283.00
UPIA-5 late-payment penalty (Audit)	\$1,947,456.60
Plus interest on tax through March 31, 2016	\$1,600,913.03
Total deficiency	* \$13,285,652.63

If you intend to pay under protest, you must pay this total deficiency amount.

Computation of balance due

Reporting period: 31-Dec-2009

Balance due	* \$13,285,652.63
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Explanation of Audit Adjustments

Income Tax



March 31, 2016

#BWNKMGV
#CNXX X161 1731 3448#

SUTHERLAND ASBILL & BRENNAN

ATTN: MARC SIMONETTI RE: IBM
1114 AVENUE OF THE AMERICAS FL 40
NEW YORK NY 10036-7703



Letter ID: CNXXX16117313448

Taxpayer ID: 13-0871985
Account ID: 16229-31968
Audit ID: A488620032
Reporting period: December 2009

Explanation of adjustments for tax period ending 12/31/2009

	<u>Income change</u>	<u>Tax impact</u>
We excluded members from your unitary group because they are an 80/20 company. [35 ILCS 5/1501(a)(27)] See attached list of the members of your unitary business group.		
We adjusted your addition modifications to reflect the correct addback of the federal bonus depreciation, or the correct reversal of the Illinois depreciation for bonus depreciation assets in the last year you are allowed a federal depreciation deduction, as required to be shown on the Form IL-4562. [35 ILCS 5/203(b)(2)(E-10), (b)(2)(E-11), (c)(2)(G-10), (c)(2)(G-11), (d)(2)(D-5), (d)(2)(D-6)]	\$600,820,322.00	\$1,667,948.00
We adjusted your subtraction modifications for foreign dividends on Schedule J, Foreign Dividends, to reflect the correct amount as allowed by Illinois law. [35 ILCS 5/203(b)(2)(G), (b)(2)(O), (h)]	\$2,289,528,326.00	\$0.00
We adjusted your subtraction modifications to reflect the correct amount of Illinois depreciation related to bonus depreciation, assets, and the reversal of the bonus depreciation addback for an asset in the last year you are allowed a federal depreciation deduction for that asset, as required to be shown on Form IL-4562. [35 ILCS 5/203(b)(2)(T), (c)(2)(R), (d)(2)(O)]	\$553,675,386.00	\$0.00
We adjusted your business income by eliminating partnership income or loss from partnerships that cannot be included in the unitary business group because they conduct 80% or more of their business activities outside the United States. [86 IL Adm. Code 100.3380(d)(3)(B)]	\$0.00	\$2,350.00
We adjusted your sales factor to include all business receipts on federal 1120, Lines 1 through 10, to the extent not expressly excluded from the sales factor. [86 IL Adm. Code 100.3370(a)(1)]	\$0.00	\$1,246.00
We adjusted/disallowed your research and development credit to reflect the correct amount as allowed by Illinois law. [35 ILCS 5/201(k)]	\$0.00	\$2,289.00

Unitary Member List

Date: March 31, 2016
Letter ID: CNXXX16117313448
Name: INTERNATIONAL BUSINESS MACHINES CORP
Taxpayer ID: 13-0871985
Account ID: 16229-31968
Audit ID: A488620032
Reporting period: December 2009
Tax period ending: 12/31/2009

<u>Name</u>	<u>FEIN</u>	<u>Status</u>
CANDLE CORP.	95-3145837	
BUILDFORGE, INC.	74-2998779	
BOWSTREET, INC.	02-0495807	
INTERNATIONAL BUSINESS MACHINES CORP.	13-0871985	
CIMS LAB, INC.	94-3322187	
CHEM SYSTEMS, INC.	13-2512931	
ASCENTIAL SYSTEMS, INC.	04-3220903	
IBM CENTRAL & EASTERN EUROPE/MID EAS	13-2672049	
IBM CREDIT FACTORING CORP.	13-3951970	
IBM CREDIT RECEIVABLES CORP.	06-1383200	
IBM CAPITAL, INC.	13-3583237	
ASCENTIAL SOFTWARE CORP.	94-3011736	
ALPHABLOX CORP.	77-0429873	
IBM WTC FINANCE LLC	06-1786227	
ACCESS360	33-0832530	
COLLATION, INC.	94-3407392	
CONSUL RISK MANAGEMENT, INC.	33-0692338	
CONTINUITY SERVICES, AN IBM CO.	22-3664236	
DATAPOWER TECHNOLOGY, INC.	04-3474247	
DSO PROPERTY CORP.	52-1683105	
ENTERPRISE INDUSTRIAL SERVICE CORP.	13-3868453	
FILENET CORP.	95-3757924	
GEMINI MANAGEMENT CORP.	13-3942383	
GSTECHNICAL SERVICES, INC.	65-1295785	
HCPG CORP.	13-3547313	
HEALTHLINK, INC.	76-0452083	
IBM OPERATIONS CORP.	13-4051710	

Unitary Member List

Date: March 31, 2016
Letter ID: CNXXX16117313448
Name: INTERNATIONAL BUSINESS MACHINES CORP
Taxpayer ID: 13-0871985
Account ID: 16229-31968
Audit ID: A488620032
Reporting period: December 2009
Tax period ending: 12/31/2009

<u>Name</u>	<u>FEIN</u>	<u>Status</u>
IBM PRINTING SYSTEMS, INC.	13-4012640	
IBM RECEIVABLES, INC.	13-3728838	
IBM RESEARCH & DEVELOPMENT, INC.	13-6104509	
IBM TRANSPORT & LOGISTICS, INC.	13-3210688	
INFORMATION LABORATORY, INC.	13-4126266	
INTERNET SECURITY SYSTEMS (GA), INC.	58-2104204	
INTERNET SECURITY SYSTEMS LATIN AMERICA	65-1151205	
INTERNET SECURITY SYSTEMS CANADA	20-3102659	
IPSS CORP.	13-3594264	
ISOGON CORP.	11-2643379	
LANGUAGE ANALYSIS SYSTEMS, INC.	54-1409090	
MICRUS HOLDINGS, INC.	14-1775306	
MICRUS HOLDINGS II, INC.	14-1817295	
MICROMUSE LATIN AMERICA, INC.	94-3401201	
CALVIN ALEXANDER NETWORKING, INC.	13-4032132	
NETOPS CORP.	06-1404431	
RIVERSOFT, INC.	13-4035689	
QUALLABY CORP.	04-3435984	
QUALLABY INTERNATIONAL, INC.	04-3466545	
GUARDEDNET, INC.	58-2512052	
MRO SOFTWARE, INC.	04-2448516	
MRO INTERNATIONAL SOFTWARE, INC.	04-2748841	
MRO INTERNATIONAL HOLDINGS, INC.	52-2010977	
NEW SOMERS MANAGEMENT, INC.	94-3290027	
NEW SOMERS II, LLC	55-0875864	
NORTH CASTLE INSURANCE, INC.	06-1719051	
PIXEL ACQUISITION CORP.	20-5951439	
IBM LENDER BUSINESS PROCESS SERVICES	20-5951227	

Unitary Member List

Date: March 31, 2016
Letter ID: CNXXX16117313448
Name: INTERNATIONAL BUSINESS MACHINES CORP
Taxpayer ID: 13-0871985
Account ID: 16229-31968
Audit ID: A488620032
Reporting period: December 2009
Tax period ending: 12/31/2009

<u>Name</u>	<u>FEIN</u>	<u>Status</u>
PV ACQUISITION CORP.	34-2024819	
IBM BUSINESS TRANSFORMATION OUTSOURCE	57-0935614	
IBM BPO HOLDINGS, INC.	59-3606014	
RATIONAL INTERNATIONAL	77-0144033	
SOFTEK STORAGE HOLDINGS, INC.	80-0101786	
SOFTEK STORAGE SOLUTIONS CORP	77-0565742	
SOFTEK STORAGE SOLUTIONS	77-0566915	
SOFTEK STORAGE SOLUTIONS (ASIA) CORP.	77-0522706	
OBJECTSTAR INTERNATIONAL, INC.	46-0485700	
SYSTEMCORP INTERNATIONAL LIMITED	06-1534653	
TECHNOLOGY SERVICE SOLUTIONS CORP.	13-3751377	
TIVOLI SYSTEMS, INC.	52-2069037	
TRELLISOFT, INC.	36-4320197	
2006 TRIDENT CO., INC.	20-4672033	
TRIGO TECHNOLOGIES, INC.	77-0533145	
WEBIFY SOLUTIONS, INC.	74-3013899	
LOTUS DEVELOPMENT INTERNATIONAL CORP.	04-2827613	
900 I AUSTIN CORP.	74-2887160	
INFORMIX DATABASE CORP.	13-4173508	
LYNX HOLDINGS, INC.	04-3614015	
WTC INSURANCE CORP., LTD.	98-0379203	
BLUEWAVE USA, INC.	13-4022053	
SPMM, INC.	75-3114969	
WATCHFIRE (USA) LIMITED	20-2446273	
WATCHFIRE, INC.	04-3518312	
PRO HOLDINGS CORPORATION	20-2446337	
WEBDIALOGS, INC	04-3393744	

Unitary Member List

Date: March 31, 2016
Letter ID: CNXXX16117313448
Name: INTERNATIONAL BUSINESS MACHINES CORP
Taxpayer ID: 13-0871985
Account ID: 16229-31968
Audit ID: A488620032
Reporting period: December 2009
Tax period ending: 12/31/2009

<u>Name</u>	<u>FEIN</u>	<u>Status</u>
NOVUS CONSULTING GROUP, INC.	54-1989025	
SOLID INFORMATION TECHNOLOGY , CORP.	77-0473446	
DMC HOLDINGS, INC	51-0378602	
DATAMIRROR, INC	51-0378461	
DATAMIRROR MOBILE SOLUTIONS, INC	77-0471278	
ENCENTUATE HOLDINGS LIMITED	20-2409472	
ENCENTUATE, INC.	04-3696404	
FILES X, INC	01-0694665	
DILIGENT TECHNOLOGIES CORPORATION	01-0704131	
PLATFORM SOLUTIONS, INC	77-0504298	
ARSENAL DIGITAL SOLUTIONS WORLDWIDE	56-2169634	
ARSENAL DIGITAL SOLUTIONS USA, INC	56-2124246	
ONE ROOM SYSTEMS, INC	56-1811617	
FILEFRENZY.COM, INC	56-2168226	
INFODYNE CORPORATION	36-3828789	
COGNOS CORPORATION	94-2763235	
APPLIX	04-2781676	
APPLIX SECURITY CORPORATION	04-3257656	
APPLIX SINGAPORE, INC	04-3329206	
VERITEAM, INC	04-3495872	
TELELOGIC HOLDING NORTH AMERICA, INC	22-3786214	
TELELOGIC NORTH AMERICA, INC	22-3411502	
TELELOGIC SYSTEMS INC	20-3629991	
POPKIN HOLDING COMPANY	13-3844611	
APPLIX CANADA INC	98-0160759	
	13-6020824	
	94-3060125	
	72-1538304	New

Unitary Member List

Date: March 31, 2016
Letter ID: CNXXX16117313448
Name: INTERNATIONAL BUSINESS MACHINES CORP
Taxpayer ID: 13-0871985
Account ID: 16229-31968
Audit ID: A488620032
Reporting period: December 2009
Tax period ending: 12/31/2009

<u>Name</u>	<u>FEIN</u>	<u>Status</u>
	80-0378525	New
	27-3050301	New
WORLD TRADE CORP	13-1602820	

Notice of Deficiency

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



March 31, 2016



Letter ID: CNXXX1677X7688X0

#BWNKMGV
#CNXX X167 7X76 88X0#
SUTHERLAND ASBILL & BRENNAN LLP

ATTN: MARC SIMONETTI RE: IBM
1114 AVENUE OF THE AMERICAS FL 40
NEW YORK NY 10036-7703

Taxpayer ID: 13-0871985
Audit ID: A488620032
Reporting period: December 2010
Total Deficiency: \$12,497,023.25
Balance due: \$12,497,023.25

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 the "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 is 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 the date 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 and administrative hearing. An administrative hearing is a formal legal proceeding conducted pursuant to the 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). 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 liability under protest using Form RR-374, Notice of Payment Under Protest (available on our website at 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 assessment total 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

cc: SUTHERLAND ASBILL & BRENNAN LLP
1114 AVE OF THE AMERICAS
NEW YORK, NY 10036

Bankruptcy Information

If you are currently under the protection of the Federal Bankruptcy Court, contact us and provide the bankruptcy number and the bankruptcy court. The bankruptcy automatic stay does not change the fact you are required to file tax returns.

Taxpayer Bill of Rights

- You have the right to call the Department of Revenue for help in resolving tax problems.
- You have the right to privacy and confidentiality under most tax laws.
- You have the right to respond, within specified time periods, to Department notices by asking questions, paying the amount due, or providing proof to refute the Department's findings.
- You have the right to appeal Department decisions, in many instances, within specified time periods, by asking for Department review, by filing a petition with the Illinois Independent Tax Tribunal, or by filing a complaint in circuit court.
- If you have overpaid your taxes, you have the right, within specified time periods, to file for a credit (or, in some cases, a refund) of that overpayment.

The full text of the Taxpayers' Bill of Rights is contained in the Illinois Compiled Statutes, 20 ILCS 2520/1 et seq.

Statement

Date: March 31, 2016
Name: INTERNATIONAL BUSINESS MACHINES CORP
Taxpayer ID: 13-0871985
Letter ID: CNXXX1677X7688X0

The attached EDA-27, Explanation of Adjustments, details your audit adjustments.

Computation of deficiency

Reporting period: 31-Dec-2010

Income or loss	
Federal taxable income	\$13,707,540,984.00
Net operating loss deduction	\$142,286,932.00
State Municipal and other interest excluded	\$7,990,778.00
Income tax and replacement tax deduction	\$23,843,315.00
Illinois bonus depreciation addition	\$767,576,353.00
Other additions	\$0.00
Base income or loss	
Foreign dividends subtraction	\$5,931,847,442.00
Illinois bonus depreciation subtraction	\$675,050,221.00
Total subtractions	\$6,606,897,663.00
Base income or net loss	\$8,042,340,699.00
Income allocable to Illinois	
Non-business income or loss	\$0.00
Non-unitary partnership bus. income or loss	\$374,090.00
Business income or loss	\$8,041,966,609.00
Apportionment formula	
Total sales everywhere	\$33,018,400,622.00
Total Illinois sales	\$1,296,682,715.00
Apportionment factor	0.039272
Business income/loss apportionable to IL	\$315,824,113.00
Nonbusiness income/loss allocable to IL	\$0.00
Non-unitary part. business income app. to IL	\$0.00
Base income or net loss allocable to IL	\$315,824,113.00
Net income	
Base income or net loss	\$315,824,113.00
IL net loss deduction (NLD)	\$0.00
Net income	\$315,824,113.00
Net replacement tax	
Replacement tax	\$7,895,603.00
Recapture of investment credits	\$0.00
Replacement tax before credits	\$7,895,603.00
Replacement tax investment credits	\$0.00
Net replacement tax	\$7,895,603.00
Net income tax	
Income tax	\$15,159,557.00

Statement

Date: March 31, 2016
Name: INTERNATIONAL BUSINESS MACHINES CORP
Taxpayer ID: 13-0871985
Letter ID: CNXXX1677X7688X0

Computation of deficiency

Reporting period: 31-Dec-2010

Recapture of investment credits	\$0.00
Income tax before credits	\$15,159,557.00
Income tax investment credits	\$531,459.00
Net income tax	\$14,628,098.00
Refund or balance due	
Net replacement tax	\$7,895,603.00
Net income tax	\$14,628,098.00
Total net income and replacement tax due	\$22,523,701.00
Minus tax previously assessed	-\$13,101,743.00
Total tax deficiency	\$9,421,958.00
UPIA-5 late-payment penalty (Audit)	\$1,884,391.60
Plus interest on tax through March 31, 2016	\$1,190,673.65
Total deficiency	* \$12,497,023.25

If you intend to pay under protest, you must pay this total deficiency amount.

Computation of balance due

Reporting period: 31-Dec-2010

Balance due	* \$12,497,023.25
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Explanation of Audit Adjustments

Income Tax



March 31, 2016

#BWNKMGV
 #CNXX XX94 XX87 3761#
 SUTHERLAND ASBILL & BRENNAN LLP
 ATTN: MARC SIMONETTI RE: IBM
 1114 AVENUE OF THE AMERICAS FL 40
 NEW YORK NY 10036-7703



Letter ID: CNXXXX94XX873761

Taxpayer ID: 13-0871985
 Account ID: 16229-31968
 Audit ID: A488620032
 Reporting period: December 2010

<u>Explanation of adjustments for tax period ending 12/31/2010</u>	<u>Income change</u>	<u>Tax impact</u>
We adjusted your Illinois net income or loss by changing the unitary group to exclude taxpayers conducting 80 percent or more of their business activities outside the United States. [35 ILCS 5/1501(a)(27)] See attached list of the members of your unitary business group.	\$0.00	\$0.00
We adjusted your addition modifications to reflect the correct addback of the federal bonus depreciation, or the correct reversal of the Illinois depreciation for bonus depreciation assets in the last year you are allowed a federal depreciation deduction, as required to be shown on the Form IL-4562. [35 ILCS 5/203(b)(2)(E-10), (b)(2)(E-11), (c)(2)(G-10), (c)(2)(G-11), (d)(2)(D-5), (d)(2)(D-6)]	\$0.00	\$0.00
We adjusted your subtraction modifications for foreign dividends on Schedule J, Foreign Dividends, to reflect the correct amount as allowed by Illinois law. [35 ILCS 5/203(b)(2)(G), (b)(2)(O), (h)]	\$4,687,137,853.00	\$0.00
We adjusted your subtraction modifications to reflect the correct amount of Illinois depreciation related to bonus depreciation, assets, and the reversal of the bonus depreciation addback for an asset in the last year you are allowed a federal depreciation deduction for that asset, as required to be shown on Form IL-4562. [35 ILCS 5/203(b)(2)(T), (c)(2)(R), (d)(2)(O)]	\$675,050,221.00	\$0.00
We adjusted your business income by eliminating partnership income or loss from partnerships that cannot be included in the unitary business group because they conduct 80% or more of their business activities outside the United States. [86 IL Adm. Code 100.3380(d)(3)(B)]	\$374,090.00	\$1,072.00
We adjusted your sales factor to include all business receipts on federal 1120, Lines 1 through 10, to the extent not expressly excluded from the sales factor. [86 IL Adm. Code 100.3370(a)(1)]	\$0.00	\$0.00
Interest on tax has been computed as allowed by Illinois law. [35ILCS 735/3-2]		
We are imposing a penalty because you did not pay the amount shown due on the Form IL-870, Waiver of Restrictions, within 30 days after the "Date of Issuance" shown on the form. Once an audit has been initiated, the late payment penalty is assessed at 15% of the late payment. Failure to pay the amount due or invoke protest rights within 30 days from the "Date of Issuance" on the Form IL-870, results in this penalty increasing to 20%. [35 ILCS 735/3-3(b-20)(2)]		

Unitary Member List

Date: March 31, 2016
Letter ID: CNXXXX94XX873761
Name: INTERNATIONAL BUSINESS MACHINES CORP
Taxpayer ID: 13-0871985
Account ID: 16229-31968
Audit ID: A488620032
Reporting period: December 2010
Tax period ending: 12/31/2010

<u>Name</u>	<u>FEIN</u>	<u>Status</u>
INTERNATIONAL BUSINESS MACHINE	13-0871985	
IBM CREDIT FACTORING CORPORATI	13-3951970	
IBM WORLD TRADE ASIA CORPORATI	13-6020824	
IBM CENTRAL & EASTERN EUROPE M	13-2672049	
IBM CAPITAL INC	13-3583237	
IBM WTC FINANCE LLC	06-1786227	
ASCENTIAL SOFTWARE CORPORATION	94-3011736	
INFORMIX INTERNATIONAL LLC	94-3060125	
CANDLE CORPORATION	95-3145837	
CONSUL RISK MANAGEMENT INC	33-0692338	
CONTINUITY SERVICES AN IBM COM	22-3664236	
DSO PROPERTY CORPORATION	52-1683105	
ENTERPRISE INDUSTRIAL SERVICE	13-3868453	
FILENET CORPORATION	95-3757924	
SPMM INC	75-3114969	
GEMINI MANAGEMENT CORPORATION	13-3942383	
GSTECHNICAL SERVICES INC	65-1295785	
HCPG CORPORATION	13-3547313	
IBM OPERATIONS CORPORATION	13-4051710	
IBM PRINTING SYSTEMS INC	13-4012640	
IBM RECEIVABLES INC	13-3728838	
IBM RESEARCH AND DEVELOPMENT I	13-6104509	
INFORMATION LABORATORY INC	13-4126266	
INTERNET SECURITY SYSTEMS GA I	58-2104204	
INTERNET SECURITY SYSTEMS CANA	20-3102659	
MICROMUSE LATIN AMERICA INC	94-3401201	
MRO SOFTWARE INC	04-2448516	

Unitary Member List

Date: March 31, 2016
Letter ID: CNXXXX94XX873761
Name: INTERNATIONAL BUSINESS MACHINES CORP
Taxpayer ID: 13-0871985
Account ID: 16229-31968
Audit ID: A488620032
Reporting period: December 2010
Tax period ending: 12/31/2010

<u>Name</u>	<u>FEIN</u>	<u>Status</u>
NEW SOMERS MANAGEMENT INC	94-3290027	
NEW SOMERS II LLC	55-0875864	
NOVUS CONSULTING GROUP INC	54-1989025	
PIXEL ACQUISITION CORP	20-5951439	
IBM LENDER BUSINESS PROCESS SE	20-5951227	
PV ACQUISITION CORP	34-2024819	
IBM BUSINESS TRANSFORMATION OU	57-0935614	
IBM BPO HOLDINGS INC	59-3606014	
RATIONAL INTERNATIONAL	77-0144033	
SOFTEK STORAGE HOLDINGS INC	80-0101786	
SOFTEK STORAGE SOLUTIONS CORP	77-0565742	
TECHNOLOGY SERVICE SOLUTIONS C	13-3751377	
TIVOLI SYSTEMS INC	52-2069037	
WATCHFIRE USA LIMITED	20-2446273	
WATCHFIRE INC	04-3518312	
WEBIFY SOLUTIONS INC	74-3013899	
WEBDIALOGS INC	04-3393744	
LOTUS DEVELOPMENT INTERNATIONA	04-2827613	
900 AUSTIN CORPORATION	74-2887160	
INFORMIX DATABASE CORPORATION	13-4173508	
LYNX HOLDINGS INC	04-3614015	
WTC INSURANCE CORPORATION LTD	98-0379203	
SOLID INFORMATION TECHNOLOGY C	77-0473446	
ENCENTUATE HOLDINGS LIMITED	20-2409472	
ENCENTUATE INC	04-3696404	
FILES X INC	01-0694665	
DILIGENT TECHNOLOGIES CORPORAT	01-0704131	
PLATFORM SOLUTIONS INC	77-0504298	

Unitary Member List

Date: March 31, 2016
Letter ID: CNXXXX94XX873761
Name: INTERNATIONAL BUSINESS MACHINES CORP
Taxpayer ID: 13-0871985
Account ID: 16229-31968
Audit ID: A488620032
Reporting period: December 2010
Tax period ending: 12/31/2010

<u>Name</u>	<u>FEIN</u>	<u>Status</u>
ARSENAL DIGITAL SOLUTIONS WORL	56-2169634	
ARSENAL DIGITAL SOLTUIONS USA	56-2124246	
INFODYNE CORPORATION	36-3828789	
COGNOS CORPORATION	94-2763235	
APPLIX INC	04-2781676	
APPLIX SINGAPORE INC	04-3329206	
VERITEAM INC	04-3495872	
TELELOGIC SYSTEMS INC	20-3629991	
POPKIN HOLDING COMPANY	13-3844611	
APPLIX CANADA INC	98-0160759	
TRANSITIVE CORPORATION	72-1538304	
IBM MEXICO HOLDINGS LLC	80-0378525	
CARLETON ACQUISITION CORP	27-3050301	
OUNCE LABS INC	20-0088187	
OUNCE LABS SECURITY CORPORATIO	74-3136451	
SPSS INC	36-2815480	New
SHOWCASE CORPORATION	41-1628214	New
NEWGENESIS CORP	04-3236862	New
SPSS TECHNOLOGY INC	26-4047233	New
SPSS US INC	31-1090815	New
LEXIQUEST INC	94-3261891	New
SURVEYCRAFT SYSTEMS INC	31-1492317	New
GUARDIUM INC	03-0487138	New
LOMBARDI SOFTWARE INC	74-2932035	New
INTELLIDEN INC	84-1542072	New
INTIATE SYSTEMS INC	36-3990887	New
ACCENX TECHNOLOGIES INC	58-2362783	New

Unitary Member List

Date: March 31, 2016
Letter ID: CNXXXX94XX873761
Name: INTERNATIONAL BUSINESS MACHINES CORP
Taxpayer ID: 13-0871985
Account ID: 16229-31968
Audit ID: A488620032
Reporting period: December 2010
Tax period ending: 12/31/2010

<u>Name</u>	<u>FEIN</u>	<u>Status</u>
TECHNOLOGY AND MANAGEMENT SERV	52-1109967	New
CAST IRON SYSTEMS INC	77-0578742	New
CORIO INC	77-0492528	New
IBM CREDIT REVOCABLE CORPORATI	06-1383200	
WORLD TRADE CORP	13-1602820	

EXHIBIT B

Sch X-1

IBM World Trade Corporation
1 Orchard Road in Armonk, NY

13-1602820

Projected rent expense

	Number of Employees	Sq Foot Needed	cost/sq ft \$15/sq ft
You need approximately 250 sq feet per employee (1)(a)			
Number of employees at IBM World Trade Corp (2)(a)	400	100,000	1,500,000
Approx. officers space 400 sq ft/officer (1)(b)	14	5,600	84,000
Reception Area (1)		300	4,500
2 Conference Rooms (25-30 sq ft/person) (30 sqft per 12 individuals)		1,080	16,200
Storage Rooms to store computers & Equip		3000	45,000
Parking Space for WTC employees		3000	45,000
Total imputed rent expense			1,694,700

Footnotes:

- a. IBM World Trade Corporation has various divisions and disregarded entities. IBM World Trade Corp Europe/Middle East/Africa This division is headquartered in Armonk. Approximate employees at this location is 400 (Source: taxpayer).
- b. IBM World Trade Corporation has 14 executives at Armonk location. (Sources: taxpayer and wiki.com getting the info from Dun & Bradstreet)

(1) approx. square feet needed per employee estimate - (Source: www.mbfinc.com)

(2) Number of employees at 1 Orchard Road Armonk, NY location (source: www.manta.com)

(3) Cost to rent office space in westchester business park, Armonk NY is \$15/sq ft. (Source: www.showcase.com)

Additional sources confirming number of Employees at Armonk location:

(5) www.hoovers.com/IBM World Trade Corp.: Lists 444 Executives at this location.

(6) www.powerprofiles.com IBM World Trade Corp: Estimated employees at this location 400

Sch X-2

Officers of IBM World Trade Corporation

Source: This list of officers is provided by IBM Co. Representative

Name of Officers	Title	Elected Date	Resigned Date	2007 Salary	2008 Salary	2009 Salary	2010 Salary
1 Joyce A Bergman (b)	Assistant Secretary	6/30/1989		1,000,000	1,020,000	1,040,000	1,060,000
2 Andrew Bonanzi (b)	Secretary	6/30/1997		500,000	520,000	530,000	540,000
3 Harsh Chugh (b)	Assistant Treasurer	4/1/2008	11/20/2009		250,000	238,333	RESIGNED
4 Douglas T. Elix (a)	Chairman, President & CEO	5/12/2004	4/1/2008	6,498,370	1,750,000	RESIGNED	RESIGNED
5 John P. Gianukakis (b)	Controller	9/30/2005	2/2/2010	400,000	415,000	430,000	37,083
6 Jesse J. Greene (b)	Treasurer	5/10/2002	10/3/2007	600,000		RESIGNED	RESIGNED
7 David L. Johnson (b)	VP Corp. Development	4/23/2001	6/11/2009	6,500,000	7,500,000	4,062,500	RESIGNED
Elias Mendoza (b)	VP Corp. Development	6/15/2009	7/21/2011			N/A	3,437,500
8 Franklin R. Kern III (b)	Chairman, President & CEO	4/1/2008	6/11/2009		6,825,000	3,927,083	RESIGNED
Virginia M. Rometty	Chairman, President & CEO	6/11/2009	1/12/2012			3,322,917	7,500,000
9 Martin Schroeter (b)	Assistant Treasurer	6/29/2007	10/3/2007	350,000		RESIGNED	RESIGNED
Martin Schroeter	Controller	2/2/2010	4/26/2010				RESIGNED
Martin Schroeter	Treasurer	10/3/2007			400,000	415,000	430,000
10 Maureen Sladek (b)	VP	11/14/2008			1,250,000	1,266,667	1,283,333
12 Gerard Vilcot (b)	Controller	10/31/1994		750,000	1,000,000	1,100,000	1,200,000
13 Daniel M Zuchelli (b)	Assistant Treasurer	5/23/2005	4/1/2008	400,000	450,000	RESIGNED	RESIGNED
Mario Vaz	Assistant Treasurer	11/20/2009				38,333	520,000
Total				16,998,370	21,380,000	16,370,833	16,007,917

(a) was derived from IBM Notice of 2008 & 2009 Annual Meeting & Proxy Statement 2007 & 2008 Summary compensation

(b) Estimate based on his or her title & years of service with Company.

Additional Officers listed on Internet : [Http://www.corporationwiki.com/New York](http://www.corporationwiki.com/New York)

1 Samuel J. Palmisano	Chairman of the Board, CEO	** Prorated 25%		6,282,682	7,135,598	6,078,449	7,929,652
2 Lucio Stanca	President	(b)		6,500,000	7,000,000	7,500,000	8,000,000
3 Greg Watson	Manager						
4 Robin Wilner	Manager						
5 Alan Ganek	V.P.						
6 John Jackson	V.P.						
7 Abby Konstamm	V.P.						

8 Robert Woods	V.P.				
9 Bruce Harreld	General Manager				
10 Grace Suh	General Manager				
11 Phil Russo	Branch Manager				
12 Tina Moon	Corporate Counsel/Legal				
13 Michelle Park	Corporate Counsel/Legal				
Grand Total			29,781,052	35,515,598	29,949,282.08 31,937,568.67

** was derived from IBM Notice of 2011 Annual Meeting & Proxy Statement - 2009 & 2010 Summary compensation

Following Officers Listed hereafter are on the internet; Power profiles.com

1 IBM World Trade Europe/Middle/East/Africa Corporation (This is a branch of IBM WTC headquartered in Armonk)

- 2 Lucio Stanca President
- 3 Librio Robeli
Joyce John Chief Finance Officers

Estimated Employees at the New York Location 400 employees.

Officers Lited on the internet: Company profile from Hoover's

- 1 Samuel J. Palmisano Chairman of the Board, CEO
- 2 Kenneth Lynch President
- 3 Owen Cropper Owner Human Resource Exec.

444 Executives listed for IBM World Trade Corporation's Armonk, NY Location

WTC is composed of various divisions: Several of the divisions are headquartered in Armonk NY: Div 50, 90,93

Taxpayer's response to IDR#4 question #9 stated : Revenue and expense booked in these divisions are attributable to activities conducted outside the U.S. Mgmt of these div. occur both in the US and non US. Example, Div 50, the employees work in Armonk, NY

The group plans & forecasts volumes by brand and product, schedules and expedites orders, monitors and tracks order status and measures inventory. The hardware products are sold to Asia Pacific Countries

80/20 computation

12/31/2009

Property Ratio

U.S. F.Assets (state by state)	Beginning	Ending	Total	Average	
Inv. Dep Assets & Land	338,379		176,920	515,299	257,650 taxpayer provided work papers
Add cap.rent exp. (see sch X-1 for detail)		0			13,557,600 (*)
Add Est.cap. leases for Exec & salesmen					1,680,000 (a)
Total U.S. Property					15,495,250

Note: Auditor used 2007 imputed amounts. In essence 2008 can be higher.

(*) Capitalized Rent Exp. (See imputed rent exp detail on Sch X-1)

(a) Conservative figure: (Average : \$350/month per car times 50 cars times 8 to capitalize)

Worldwide F.A.(U.S. 1120)	Beginning	Ending	Total	Average	
Inv, Dep. Assets & Land	71,491,740		61,829,946	133,321,686	66,660,843 US 1120 B.S.
Add Cap. Rent Exp. US 1120 Line 16 (2,210,534*8)					17,684,272 US 1120 Line 16
Add Total U. S. prop. Including imputed amount					15,495,250
Less: Inv Dep Assets & Land included in U.S. that's included in Everywhere					(257,650)
Total Property Everywhere					99,582,715

Property Factor: US. Property/Everywhere Property for 80/20 test **0.155602**

U.S. Payroll

Payroll Ratio

U.S. Payroll provided by the taxpayer	1,250,270
Add: Sal. & Wages for Officers of WTC & prorated Portion of IBM's Chairman	29,949,282 Sch X-2
Add: Cost of Salaries paid by WTC for cost sharing in the R&D (b)	- (b)
Total U.S. Payroll	31,199,552

(b) IBM Corporation's Salaries claimed for R&D Tax credit are excluded from WTC 80/20 calculation

80/20 computation

Payroll Ratio

12/31/2009

Everywhere Payroll

Total payroll claimed on U.S. 1120	16,955,704
Less: U.S. payroll included in the above amt.	(1,250,270)
Add: Total U.S. Payroll & Officers Comp including imputed amt.	31,199,552
 Grand Total of Payroll Everywhere	 46,904,986
 Payroll Factor: US. Payroll/Everywhere Payroll for 80/20 test	 0.665165
 Average property & payroll U.S./Everywhere for 80/20 test	 0.410383367

80/20 computation

12/31/2010

Property Ratio

U.S. F.Assets (state by state)	Beginning	Ending	Total	Average	
Inv. Dep Assets & Land	176,920		8,887	185,807	92,904 taxpayer provided work papers
Add cap.rent exp. (see sch X-1 for detail)		0			13,557,600 (*)
Add Est.cap. leases for Exec & salesmen					1,680,000 (a)
Total U.S. Property					15,330,504

Note: Auditor used 2007 imputed amounts. In essence 2008 can be higher.

(*) Capitalized Rent Exp. (See imputed rent exp detail on Sch X-1)

(a) Conservative figure: (Average : \$350/month per car times 50 cars times 8 to capitalize)

Worldwide F.A.(U.S. 1120)	Beginning	Ending	Total	Average	
Inv, Dep. Assets & Land	61,829,946		70,172,287	132,002,233	66,001,117 US 1120 B.S.
Add Cap. Rent Exp. US 1120 Line 16 (2,591,204*8)					20,729,632 US 1120 Line 16
Add Total U. S. prop. Including imputed amount					15,330,504
Less: Inv Dep Assets & Land included in U.S. that's included in Everywhere					(92,904)
Total Property Everywhere					101,968,349

Property Factor: US. Property/Everywhere Property for 80/20 test

0.150346

U.S. Payroll

U.S. Payroll provided by the taxpayer	
Add: Sal. & Wages for Officers of WTC & prorated Portion of IBM's Chairman	
Add: Cost of Salaries paid by WTC for cost sharing in the R&D (b)	
Total U.S. Payroll	

Payroll Ratio

	336,499	
	31,937,569	Sch X-2
	-	(b)
Total	32,274,068	

(b) IBM Corporation's Salaries claimed for R&D Tax credit are excluded from WTC 80/20 calculation

80/20 computation

Property Ratio

12/31/2010

Everywhere Payroll

Total payroll claimed on U.S. 1120	17,732,324
Less: U.S. payroll included in the above amt.	(336,499)
Add: Total U.S. Payroll & Officers Comp including imputed amt.	32,274,068
 Grand Total of Payroll Everywhere	 49,669,893
 Payroll Factor: US. Payroll/Everywhere Payroll for 80/20 test	 0.649771
 Average property & payroll U.S./Everywhere for 80/20 test	 0.400058473

EXHIBIT C

From: Callahan, Craig <Craig.Callahan@Illinois.gov>
Sent: Tuesday, January 19, 2016 1:47 PM
To: Appleby, Andrew
Cc: Fliflet, Brian
Subject: Illinois ICB Review - IBM - Audit Period 1/1/2009-12/31/2010

Andrew:

I understand IBM recently received an Action Decision, which denied relief requested for the audit period 1/1/2009 – 12/31/2010. This morning I reviewed the ICB case file and read my June 10, 2015 Action Plan e-mail to you and Mark (a copy is below). To execute the same, I recall that I discussed the “audit file 80/20 test information” with the audit team, reviewed the documents you presented at the informal conference, and concluded there was no additional information needed by the Informal Conference Board for its deliberation of IBM’s objections to the Notice of Proposed Deficiency. Therefore, I did not send you a request for additional information.

During today’s telephone conversation you reminded me that shortly after we convened the June 10, 2015 in-person informal conference, two of the three Board members excused themselves from the conference. The reason may have been a request from the Governor. Given the diminished audience on June 10, 2015, I understand you would like to present that same information and possibly additional information to the three Board members as soon as possible.

I will submit your request to Brian Fliflet, ICB Administrator.

Best regards,

Craig

Craig W. Callahan
ICB Conferee
(312) 814-4942

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From: Appleby, Andrew [mailto:Andrew.Appleby@sutherland.com]
Sent: Tuesday, January 19, 2016 11:28 AM
To: Callahan, Craig
Subject: FW: Illinois ICB Review - IBM - Audit Period 1/1/2009-12/31/2010 - Action Plan

Mr. Callahan,

Below please find the email chain from June regarding the IBM ICB hearing for 2009-2010. As I mentioned on the phone today, we had agreed to adjourn the hearing because two members of the Board had to exit the hearing after just a few minutes. Our understanding, based on that discussion and the email below, was that we were waiting for a follow up information request from the ICB and that we would have a full ICB hearing once we provided responses to that request.

Thanks again,

Andrew Appleby | *Counsel* | 212.389.5042

www.stateandlocaltax.com

From: Simonetti, Marc

Sent: Thursday, June 11, 2015 11:29 AM

To: Callahan, Craig; Appleby, Andrew

Cc: Calvert, Louise; Atherley, Troy

Subject: RE: Illinois ICB Review - IBM - Audit Period 1/1/2009-12/31/2010 - Action Plan

Craig,

Thank you. We are glad to supply additional information that would be helpful for you to determine WTC is an 80/20 entity.

We look forward to hearing back from you. Thanks.

Marc Simonetti | *Partner* | 212.389.5015

www.stateandlocaltax.com

From: Callahan, Craig [<mailto:Craig.Callahan@Illinois.gov>]

Sent: Wednesday, June 10, 2015 3:51 PM

To: Simonetti, Marc; Appleby, Andrew

Cc: Calvert, Louise; Atherley, Troy

Subject: Illinois ICB Review - IBM - Audit Period 1/1/2009-12/31/2010 - Action Plan

Mark and Andrew:

This afternoon I spoke to the auditor. He will send me a list of the "80/20 test" documentation provided by the taxpayer. I will discuss the same with the audit team, and identify any additional information we need before the Board can determine if WTC "proved clearly" that it is entitled to the 80/20 exemption – the threshold of proof referred to by the *Zebra* appellate court. I will submit that list of additional information to you, after which we can convene a short conference call to discuss how to proceed at the ICB.

Best regards,

Craig

Craig W. Callahan

ICB Conferee

(312) 814-4942

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