IN THE ILLINOIS INDEPENDENT TAX TRIBUNAL

VODAFONE USA PARTNERS & AFFILIATES and VODAFONE AMERICAS HOLDINGS INC. & AFFILIATES	)	
Petitioner,	)	
v.	)	No. 14 TT 23
THE ILLINOIS DEPARTMENT OF REVENUE,	)	
Defendant.	)	

RECEIVED
FEB 26 2014
BY:

PETITION

Petitioner, Vodafone USA Partners & Affiliates and Vodafone Americas Holdings, Inc. & Affiliates ("Petitioners"), by and through its attorneys, Horwood Marcus & Berk Chartered, complains of the Defendant, the Illinois Department of Revenue ("Department"), and alleges as follows:

PARTIES

1. Petitioner is headquartered at Denver Place South Tower, 999 18th Street, Suite 1750, Denver, Colorado, 80202-2404.

2. Petitioner is represented by Horwood Marcus & Berk Chartered attorneys Marilyn A. Wethekam and Breen M. Schiller located at 500 West Madison St., Suite 3700, Chicago, Illinois 60661, and can be reached at 312-606-3240 or mwetheka@hmblaw.com; and 312-606-3220 or bschiller@hmblaw.com, respectively.

3. Petitioner's FEIN is 52-2207068 .

4. Petitioner's Illinois Account Number is 3261-2192.

5. 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.

NOTICES

6. On December 31, 2013, and January 21, 2014 the Department issued Petitioner Notices of Claim Denial ("Notices") for the taxable years ending March 31, 2005, March 31, 2006 and March 31, 2007 ("Years at Issue") denying Petitioner's claims for refund of its Illinois corporate income tax overpayments in the following amounts: $764,876.00; $1,642,057.00; and $5,141,601.00, respectively.

7. True and accurate copies of the Notices are attached hereto as Exhibit A.

8. The total amount denied for the Years at Issue is $7,548,534.00.

JURISDICTION

9. 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.

10. This 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.

BACKGROUND

11. The tax involved herein is the Illinois corporate income and replacement tax imposed under the Illinois Income Tax Act (the "Act"), 35 ILCS §5/201, et seq.

12. Petitioner's is a partner in Cellco Partnership ("Cellco") with six unrelated Verizon Wireless entities.

13. Cellco and its subsidiaries do business as "Verizon Wireless."

14. Petitioner's activities in the United States are limited to its forty-five percent (45%) ownership of Cellco.

15. Cellco's sales relate to the provision of intangible telecommunication services in the form of voice and data services, and certain sales stemming from the sale of equipment (tangible personal property), such as handsets.

16. Cellco calculated its sales factor apportionment formula for all states, including Illinois, utilizing a primary place of use ("PPU") methodology.

17. The PPU methodology sources receipts to a state based upon the physical location of the customers located within the state.

18. A customer's PPU is determined by the customer's billing address.

19. Historically, Petitioner calculated its Illinois sales factor consistent with Cellco.

CONTROVERSY

20. On its original returns for the Years at Issue ("Original Returns"), Petitioner sourced its receipts related to its provision of telecommunication services on a PPU basis opposed to the cost of performance methodology as required by Illinois law. 35 ILCS §5/304(a)(3)(C)(i-ii); 86 Ill. Admin. Code §100.3370(c)(3)(A).

21. As part of an apportionment study that analyzed the proper method of sourcing receipts for apportionment factor purposes in all states, Petitioner determined that it had been incorrectly sourcing receipts to Illinois.

22. Petitioner sought the advice of an outside, third-party, expert tax-consulting firm to conduct the apportionment study.

23. As a result, Petitioner amended its Illinois corporate income and replacement tax returns ("Amended Returns") for the Years at Issue.

24. Petitioner's basis for filing Amended Returns was that its Original Returns were filed incorrectly using the PPU methodology which is akin to a market-based approach.

25. Petitioner's revised amount of tax due on its Amended Returns was calculated using Illinois's statutory cost of performance methodology in place during the Years at Issue.

26. Petitioner's sales factor was revised in order to (i) accurately reflect the amount of net sales in Illinois based on cost of performance resulting from Petitioner's "income-producing activities," and (ii) be consistent with the Illinois statute. *Id*

27. Upon review of Petitioner's Amended Returns, the Department denied Petitioner's apportionment factor revisions.

28. The Department adjusted Petitioner's Illinois sales factor to include receipts as determined by the PPU methodology as originally reported on Petitioner's Original Returns.

29. On December 31, 2013, and January 16, 2014, the Department issued Petitioner Notices for the Years at Issue.

COUNT I
Pursuant to Illinois law, Petitioner properly sourced its Income to Illinois on a cost of performance basis during the Years at Issue.

30. Petitioner realleges and incorporates by this reference the allegations made in paragraphs 1 through 29.

31. A multistate taxpayer divides its taxable profits between Illinois and the other jurisdictions where it operates by multiplying its net income by an "apportionment" percentage. 35 ILCS 5/304(a).

32. During the Years at Issue, the percentage was based solely on the sales factor.

33. The sales factor is the ratio of the taxpayer's total sales in this State during the taxable period over the taxpayer's total sales everywhere during the taxable period. 35 ILCS 5/304(a)(3)(A).

34. For purposes of calculating a taxpayer's Illinois sales factor for sales other than the sale of tangible personal property during the Years at Issue, Illinois followed a pure "cost of performance" model. 35 ILCS §5/304(a)(3)(C)(i-ii); 86 Ill. Admin. Code §100.3370(c)(3)(A).

35. With respect to sales other than sales of tangible personal property, *e.g.*, sales of communications services, a taxpayer's sales are "in this State" if the taxpayer's income-producing activity is performed both inside and outside Illinois, and the greater proportion of the activity is performed inside Illinois than outside Illinois, based on the costs of performing the activities. 35 ILCS 5/304(a)(3)(C)(ii).

36. "Income producing activity" was defined as transactions and activity directly engaged in by the person in the regular course of its trade or business for the ultimate purpose of gain or profit. 86 Ill. Admin. Code §100.3370(c)(3)(A).

37. Cellco's principal income-producing activities during the Years at Issue consisted of providing telecommunications and data services.

38. Therefore, 35 ILCS §5/304(a)(3)(C) controls the determination of whether and to what extent earnings received from the sales of Cellco's telecommunication and data services should be attributed to Illinois for purposes of calculating Petitioner's Illinois sales factor.

39. On its Original Return, Petitioner sourced Illinois earnings based upon the billing address (market-based) of the customer to whom the services were sold.

40. Petitioner filed an Amended Returns for the Years at Issue to reflect the proper Illinois apportionment factor.

41. On its Amended Return, Petitioner's Illinois sales factor was adjusted to accurately reflect the amount of net sales in Illinois based on cost of performance, Illinois's statutorily required sourcing method during the Years at Issue.

42. Upon audit, the Department denied Petitioner's adjustments.

43. Petitioner's sourcing method on its Original Return was incorrect and contrary to the cost of performance method required by Illinois law during the Years at Issue.

44. Illinois did not move to a market-based approach for the sourcing of sales to the State until tax years beginning on or after December 31, 2008. 35 ILCS §5/304(a)(3)(C-5).

45. By using the billing address of Cellco's customers to source earnings from the sale of Cellco's telecommunications services to Illinois, Petitioner attributed a substantially greater amount of those earnings to Illinois than should have been attributed by the statutorily required cost of performance method.

46. During the Years at Issue, more than 50% of Cellco's direct costs of performance for its telecommunication and data services occurred outside of Illinois.

47. As a result, the revenue associated with these sales should be excluded from the numerator of Petitioner's Illinois sales factor.

48. Accordingly, Petitioner properly sourced its income to Illinois on a cost of performance basis and the Department's re-allocation of 100% of Petitioner's income to Illinois was improper.

49. The Department's proposed sales factor adjustment is contrary to the law and is not supported by the facts.

WHEREFORE, Petitioner prays that this Tribunal enter an Order that:

a. finds and declares that Petitioner properly sourced its income to Illinois pursuant to a cost of performance basis pursuant to 35 ILCS §5/304(a)(3)(C)(i-ii) and 35 ILCS §5/304(a)(3)(C-5)(iii)(b);

b. finds and declares that the Department's adjustment to Petitioner's sales factor numerator pursuant to a market-based sourcing methodology for the Years at Issue was improper;

c. finds and declares that the Department's denial of Petitioner's Amended Returns was erroneous; and

d. grants such further relief as this Tribunal deems appropriate under the circumstances.

COUNT II

The Department erred in adjusting Petitioner's apportionment factor because the Department's method taxes extraterritorial values by attributing income to Illinois which is <u>out of all appropriate proportion to the business transacted in Illinois.</u>

50. Petitioner realleges and incorporates by this reference the allegations made in paragraphs 1 through 49, inclusive, hereinabove.

51. The purpose of the apportionment formula is to assign profits to Illinois in proportion to the level of business activity a taxpayer conducts in the state. *Continental Illinois Nat'l Bank and Trust v. Lenckos,* 102 Ill. 2d 210, 224 (1984); *Caterpillar Tractor Co. v. Lenckos,* 84 Ill. 2d 102, 123 (1981) (the purpose of the formula is to confine the taxation of income to the portion of the total income that is attributable to local activities).

52. On its Amended Returns, Petitioner sourced Cellco's Illinois earnings based on the cost of performance methodology as required by Illinois law.

53. The majority of the costs of performance for Cellco's telecommunication and data services occurred outside of Illinois.

54. As a result, the revenue associated with these sales was excluded from the numerator of Petitioner's Amended Illinois sales factor.

55. Upon audit, the Department denied Petitioner's adjustments and reallocated Cellco's sales to Illinois based on the billing address of the customer, i.e., a market-based sourcing methodology.

56. Illinois did not move to a market-based approach for the sourcing of sales to the State until tax years beginning on or after December 31, 2008. 35 ILCS §5/304(a)(3)(C-5).

57. By using the billing address of Cellco's customers to source earnings from the sale of Cellco's telecommunications services to Illinois, Petitioner attributed a substantially greater amount of those earnings to Illinois than should have been attributed by the statutorily required cost of performance method.

58. The use of the Department's method is inappropriate because it assigns income to Illinois that is out of all appropriate proportion to Petitioner's in-state income-producing activities.

59. Accordingly, the Department erred in adjusting Petitioner's Illinois apportionment factor for the Years at Issue.

WHEREFORE, Petitioner prays that this Tribunal enter an Order that:

a. finds and declares that Petitioner properly sourced its income to Illinois pursuant to a cost of performance basis pursuant to 35 ILCS §5/304(a)(3)(C)(i-ii) and 35 ILCS §5/304(a)(3)(C-5)(iii)(b);

b. finds and declares that the Department's re-allocation of Cellco's sales for the Years at Issue based on the billing address of the customer was improper and out of all appropriate proportion to Petitioner's business transacted in Illinois;

c. finds and declares that the Department's denial of Petitioner's Amended Returns was erroneous; and

d. grants such further relief as this Tribunal deems appropriate under the circumstances.

COUNT III
Pursuant to 35 ILCS §5/305(c), Petitioner was required to apportion its partnership income in the same manner as any other nonresident.

60. Petitioner realleges and reincorporates the allegations in paragraphs 1 through 59, inclusive, hereinabove.

61. Under Illinois law, a partnership is a "contractual relationship of mutual agency which is formed to carry on a business purpose." *Acker v. Dep't. of Rev.,* 116 Ill. App. 1080, 1083 (1st Dist. 1983).

62. For Illinois income tax purposes, the partnership is regarded as an independently recognizable entity apart from the aggregate of its partners" whose income is taxed to each partner as if "the partnership was merely an agent or a conduit through which the income passed." *Id.*

63. As such, each partner is entitled to a distribute share of the partnership income from every source and should be taxed on that basis.

64. Specifically, Section 305(c) provides that "base income of a partnership shall be allocated or apportioned to this State pursuant to Article 3, in the same manner as it is allocated or apportioned for any other nonresident." 35 ILCS §5/305(c); 86 Ill. Admin. Code

§100.3500(b)(2); *See Also, BP Oil Pipeline Co. v. Bower,* Docket No. 1-01-2364 (Ill App. 1st Dist.) (5/21/2004); *Exxon Corp. v. Bower,* Docket No. 1-01-3302 (Ill App. 1st Dist.) (5/21/2004).

65. Here, for purposes of calculating a nonresident-taxpayer's Illinois sales factor for sales other than the sale of tangible personal property during the Years at Issue, Illinois followed a pure "cost of performance" model. 35 ILCS §5/304(a)(3)(C)(i-ii); 86 Ill. Admin. Code §100.3370(c)(3)(A).

66. Accordingly, Petitioner was required to calculate the numerator of its Illinois sales factor on a cost of performance basis for the Years at Issue.

67. Petitioner's Amended Returns were filed in accordance with Illinois law in effect during the Years at Issue.

68. The Department's denial of Petitioner's adjustments and issuance of its Notices was erroneous.

WHEREFORE, Petitioner prays that the Tribunal enter an Order that:

a. finds and declares that pursuant to 35 ILCS §5/305(c), base income of a partnership shall be allocated or apportioned to this State pursuant to Article 3, in the same manner as it is allocated or apportioned for any other nonresident.

b. finds and declares that Petitioner filed its Amended Returns pursuant to the required sourcing methodology of 35 ILCS §5/304(a)(3)(C);

c. finds and declares that the Department's denial of Petitioner's Amended Returns was erroneous; and

d. grants such further relief as this Tribunal deems appropriate under the circumstances.

Respectfully Submitted,
VODAFONE USA PARTNERS & AFFILIATES and VODAFONE AMERICAS HOLDINGS INC. & AFFILIATES
Petitioner

By: Breen M. Schiller
One of its Attorneys

Marilyn A. Wethekam
Breen M. Schiller
HORWOOD MARCUS & BERK CHARTERED
500 West Madison Street, Suite 3700
Chicago, Illinois 60661
(312) 606-3200

Illinois Department of Revenue
101 W. Jefferson St.
Springfield, IL 62702

RECEIVED
JAN 21 2014
BY: TS

NOTICE OF DENIAL

#2832

01/16/2014

FORM: IL-1120
TRACK NUMBER: A1698597376

VODAFONE USA PTRS & AFFILIATES
VODAFONE AMERICAS HOLDINGS INC & AFFILIATES
SUITE 1750
DENVER PLACE SOUTH TOWER
999 18TH ST
DENVER CO 80202-2404

FEIN: 52-2207068

TAXABLE YEAR ENDING
03/31/2005

AMOUNT DENIED
$764,876.00

Pursuant to Section 909(e) of the Illinois Income Tax Act, notice is hereby given that your claims for refund of income tax overpayment in the amount of $764,876.00 for the taxable year ending 03/31/2005 filed on 01/09/2009 is denied in full.

IF YOU DO NOT AGREE, Section 910(a) of the Act provides that the Department shall reconsider the denial if within 60 days of the date of this notice, the claimant or his authorized representative files a written protest setting forth the grounds upon which the protest is based and, if requested, shall grant the taxpayer or his authorized representative a hearing (under Section 914). Thus, if you disagree with the proposed denial of your claim, you may file a protest and, if desired, request a hearing. If an adequate and timely protest is not received, the denial of your claim to the extent shown above will become final as of the expiration of the aforementioned 60-day period pursuant to Section 909(f). A protest, if filed, should be forwarded to the address shown below.

Sincerely,

Brian Hamer
Director

Enclosures: EAR-14
IDR-867
Return Envelope

NOTICE SECTION
ILLINOIS DEPARTMENT OF REVENUE
PO BOX 19012
SPRINGFIELD, IL 62794-9012
PHONE: 217 524-5292
ATTENTION: JAR A1698597376

STATEMENT

VODAFONE USA PTRS & AFFILIATES
VODAFONE AMERICAS HOLDINGS INC & AFFILIATES
SUITE 1750
DENVER PLACE SOUTH TOWER
999 18TH ST
DENVER CO 80202-2404

TAXABLE YEAR ENDING
03/31/2005
TRACK NUMBER: A1698597376

Pursuant to Section 909(e) of the Illinois Income Tax Act, notice is hereby given that your claim for refund of income tax overpayment in the amount of $764,876.00 for the taxable year ending 03/31/2005 filed on 01/09/2009 is denied in full. The Department holds the tax as determined by the audit examination concluded on 08/20/2013 to be the correct liability for these years and thus finds no tax overpayment to exist.

Illinois Department of Revenue
101 W. Jefferson St.
Springfield, IL 62702

NOTICE OF DENIAL

12/31/2013

FORM: IL-1120
TRACK NUMBER: A266186752

VODAFONE USA PTRS & AFFILIATES
VODAFONE AMERICAS HOLDINGS INC & AFFILIATES
SUITE 1750
DENVER PLACE SOUTH TOWER
999 18TH ST
DENVER CO 80202-2404

FEIN: 52-2207068

TAXABLE YEARS ENDING
03/31/2006 AND 03/31/2007

AMOUNT DENIED
$6,783,658.00

Pursuant to Section 909(e) of the Illinois Income Tax Act, notice is hereby given that your claims for refund of income tax overpayments in the amounts of $1,642,057.00 for the taxable year ending 03/31/2006 filed on 06/05/2009 and $5,141,601.00 for taxable year ending 03/31/2007 filed on 06/05/2009 are denied in full.

IF YOU DO NOT AGREE, Section 910(a) of the Act provides that the Department shall reconsider the denial if within 60 days of the date of this notice, the claimant or his authorized representative files a written protest setting forth the grounds upon which the protest is based and, if requested, shall grant the taxpayer or his authorized representative a hearing (under Section 914). Thus, if you disagree with the proposed denial of your claim, you may file a protest and, if desired, request a hearing. If an adequate and timely protest is not received, the denial of your claim to the extent shown above will become final as of the expiration of the aforementioned 60-day period pursuant to Section 909(f). A protest, if filed, should be forwarded to the address shown below.

Sincerely,

Brian Hamer
Director

Enclosures: EAR-14
IDR-867
Return Envelope

NOTICE SECTION
ILLINOIS DEPARTMENT OF REVENUE
PO BOX 19012
SPRINGFIELD, IL 62794-9012
PHONE: 217 524-5292
ATTENTION: JAR A266186752

STATEMENT

VODAFONE USA PTRS & AFFILIATES
VODAFONE AMERICAS HOLDINGS INC & AFFILIATES
SUITE 1750
DENVER PLACE SOUTH TOWER
999 18TH ST
DENVER CO 80202-2404

TAXABLE YEARS ENDING
03/31/2006 AND 03/31/2007
TRACK NUMBER: A266186752

Pursuant to Section 909(e) of the Illinois Income Tax Act, notice is hereby given that your claims for refund of income tax overpayments in the amounts of $1,642,057.00 for the taxable year ending 03/31/2006 filed on 06/05/2009 and $5,141,601.00 for taxable year ending 03/31/2007 filed on 06/05/2009 are denied in full. The Department holds the tax as determined by the audit examination concluded on 08/20/2013 to be the correct liability for these years and thus finds no tax overpayment to exist.

CERTIFICATE OF SERVICE

Undersigned counsel of record hereby certifies that she caused a copy of the foregoing **Petition** to be served upon other counsel of record herein by causing the same to be placed in an envelope, properly addressed and deposited in the U.S. Mail at 500 W. Madison, Chicago, IL 60661 before the hour of 5:00 p.m. on the 26th day of February, 2014.

Illinois Department of Revenue
Office of Legal Services
100 W. Randolph St., 7-900
Chicago, IL 60601

Bren M. Schiller