

World Trade Corporation (“WTC”), a wholly-owned subsidiary of IBM, to recharacterize WTC from an excluded entity (*i.e.*, an “80/20 Company”) to an entity included in IBM’s Illinois unitary combined returns for the tax years ended December 31, 2007 and December 31, 2008.

3. As a matter of law, the Department does not have the legal authority to impute property or payroll for purposes of determining whether an entity is classified as an 80/20 Company.

4. IBM incorporates its Memorandum of Law in Support of its Motion for Summary Judgment as if fully set forth in this paragraph.

5. Since there is no genuine issue of material fact to be decided by the Tribunal, summary judgment should be granted in favor of IBM.

WHEREFORE, IBM requests this Tribunal enter an order:

- a) Granting IBM’s Motion for Summary Judgment;
- b) Holding that the Department does not have the legal authority to impute property or payroll for purposes of determining whether an entity constitutes an 80/20 Company excluded from the Illinois unitary combined return;
- c) Holding that the Notices of Deficiency, dated September 24, 2014, issued by the Department to IBM assessing a total balance due of \$15,641,342.00 in tax, \$6,256,536.80 in penalty, and \$6,024,387.88 in interest for the tax years ended December 31, 2007 and December 31, 2008, are erroneous, improper, and void; and
- d) Any further review this Tribunal deems just.

Respectfully submitted,

SUTHERLAND ASBILL & BRENNAN LLP
Attorneys for Petitioner

By: _____

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DATED: March 19, 2015

Illinois tax law expressly provides that an entity whose business activity outside the United States is 80% or more of that entity's total business activity (commonly referred to as an "80/20 Company") cannot be included in an Illinois unitary combined return. 35 Ill. Comp. Stat. 5/1501(a)(27)(A). To determine whether an entity is an 80/20 Company, Illinois tax law requires the comparison of that entity's United States business activity to worldwide business activity, and analyzes that entity's property and payroll ("80/20 Test"). 35 Ill. Comp. Stat. 5/1501(a)(27)(A); Ill. Admin. Code tit. 86, § 100.9700(c).

IBM correctly determined that IBM World Trade Corporation ("WTC"), a wholly-owned subsidiary of IBM, constituted an 80/20 Company that must be excluded from IBM's Illinois unitary combined returns for the tax years ended December 31, 2007 and December 31, 2008 ("Years at Issue"). IBM provided support for WTC's 80/20 Test calculation both in its tax returns and throughout the audit.

The Department audited IBM's corporate income tax returns for the Years at Issue and issued an assessment of additional tax asserting that WTC did not constitute an 80/20 Company. It is undisputed that, if the property or payroll the Department imputed, or allocated, from IBM to WTC is not considered, WTC constitutes an 80/20 Company and must be excluded from IBM's Illinois unitary combined returns for the Years at Issue. The Department did not contest the property and payroll figures WTC reported and provided. Rather, to disregard WTC's statutory characterization as an 80/20 Company, the Department imputed, or allocated, additional property and payroll from IBM to WTC. But Illinois law does not grant the Department the legal authority to impute property or payroll for purposes of the 80/20 Test. The Department's adjustments result in impermissible *ultra vires* lawmaking.

There are no material facts in dispute related to the issue in this Motion for Summary

Judgment. As such, summary judgment is appropriate here. 735 Ill. Comp. Stat. 5/2-1005. The Department does not have legal authority to impute property and payroll for purposes of the 80/20 Test. Therefore, this Tribunal must grant IBM's Motion for Summary Judgment.

II. FACTS

1. WTC is a Delaware corporation with its headquarters in New York. *See* Answer ¶ 9.
2. The Department audited IBM's income tax returns for the Years at Issue. *See* Answer ¶ 30.
3. During the audit, IBM provided the Department with W-2 Forms that illustrated WTC had 20 employees in the U.S., and illustrated the payroll for those employees. *See* Answer ¶¶ 22, 41.
4. In 2007 and 2008, WTC operated a network of foreign branches that employed hundreds of employees and at least fifty contractors outside the United States. *See* Answer ¶¶ 23.
5. During the audit, IBM provided the Department with documentation that illustrated WTC's U.S. property for the Years at Issue. *See* Auditor Workpapers ("Workpapers"), Schedules X-1 and X-3.
6. During the audit, IBM provided tax return documentation that reflected WTC's everywhere property and payroll.
7. Pursuant to the documentation and tax returns, WTC qualified as an 80/20 Company.

8. Nevertheless, the Department issued an assessment of additional tax because the Department disregarded WTC's statutory classification as an 80/20 Company. *See Answer ¶ 32.*
9. The Department provided workpapers containing its assumptions and calculations for the 80/20 Test. A copy of the Workpapers is attached as **Exhibit A**. *See Answer ¶ 34.*
10. The Department imputed U.S. property and payroll from IBM to WTC for purposes of the 80/20 Test. *See Answer ¶¶ 33, 34, 52; Workpapers, Schedules X-1, X-2, and X-3.*
11. 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 payroll and property fractions. *See Answer ¶¶ 40, 87.*
12. The Department's sole basis to disregard WTC's statutory characterization as an 80/20 Company was the imputation of property and payroll from IBM to WTC. *See Answer ¶¶ 32-34; Workpapers, Schedules X-1, X-2, and X-3.*
13. Without the imputation of U.S. property and payroll from IBM to WTC, the Department agrees with WTC's statutory classification as an 80/20 Company. *See Workpapers, Schedules X-1, X-2, and X-3.*
14. On September 24, 2014, the Department issued Notices of Deficiency ("Notices") to IBM assessing a total balance due of \$15,641,342.00 in tax, \$6,256,536.80 in penalty, and \$6,024,387.88 in interest for the tax years ended December 31, 2007 and December 31, 2008. A copy of the Notices is attached as **Exhibit B**. *See Answer ¶ 7.*

III. ARGUMENT

A. Standard of Review for Summary Judgment

A motion for summary judgment is appropriate where the pleadings, affidavits, and other documents on file show that there is no genuine issue as to any material fact on a particular issue and that the moving party is entitled to judgment as a matter of law. 735 Ill. Comp. Stat. 5/2-1005(c); *People ex rel. Dep't of Revenue v. Nat'l Liquors Empire, Inc.*, 157 Ill. App. 3d 434, 437-438 (4th Dist. 1987). Summary judgment is also appropriate where the parties agree on the facts, but dispute the construction of an applicable statute. *Bezan v. Chrysler Motors Corp.*, 263 Ill. App. 3d 858, 864 (2d Dist. 1994).

B. The Department Does Not Have the Authority to Impute Property or Payroll to WTC for the 80/20 Test

Illinois statutes expressly mandate which entities are included in a combined return, and how to determine if an entity is an excluded 80/20 Company. Illinois tax law provides no authority to deviate from these statutory mandates. The Department cannot impute property or payroll from one entity to another to disregard the statutory classification of an entity as an 80/20 Company in contravention of Illinois tax law.

Illinois tax law expressly 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). 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. 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). 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, *i.e.*, an 80/20 Company, as set forth in Illinois statute. *Id.*; *see also Dover Corp. v. Illinois Dep't of*

Revenue, No.98 L 50170 (Ill. Cir. Ct. Cook Jan. 14, 2000) (granting summary judgment excluding an 80/20 Company as a matter of law).

Illinois tax law requires the taxpayer to compare United States business activity to worldwide business activity for each entity, *i.e.*, the 80/20 Test. 35 Ill. Comp. Stat. 5/1501(a)(27)(A); Ill. Admin. Code tit. 86, § 100.9700(c). The 80/20 Test involves two fractions—property and payroll. 35 Ill. Comp. Stat. 5/1501(a)(27)(A); Ill. Admin. Code tit. 86, § 100.9700(c). Pursuant to Illinois statute, the numerators of the fractions represent that entity’s property and payroll from sources within the United States, and the denominators of the fractions represent that entity’s respective worldwide property and payroll.¹ 35 Ill. Comp. Stat. 5/1501(a)(27)(A); Ill. Admin. Code tit. 86, § 100.9700(c). 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). The taxpayer must compute each entity’s property and payroll fractions using the calculation set forth in Illinois statute. *Id.* A taxpayer must average the two fractions to arrive at its business activity fraction. *Id.* No Illinois statute provides any authority for the Department or a taxpayer to deviate from the statutory 80/20 Test calculation.²

i. The Department Does Not Have the Authority to Impute Payroll to WTC for the 80/20 Test

Illinois tax law mandates that an entity’s payroll fraction is a fraction comprised of a numerator, which is that entity’s total compensation paid within the United States during the taxable year; and a denominator, which is that entity’s total compensation paid everywhere

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 equals or exceeds 80%.

² In fact, “[n]one of the Department’s regulations...expressly authorize the reallocation the Department proposes here.” *Ill. Dep’t of Revenue v. Shanghai, Inc.*, IT 02-1 (Office of Admin. Hearings Feb. 7, 2002) (emphasis added).

during the taxable year. 35 Ill. Comp. Stat. 5/1501(a)(27)(A); 35 Ill. Comp. Stat. 5/304(a)(2)(A). 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.” Ill. Admin. Code tit. 86, § 100.3100(b); *see also*, *Ill. Dep’t of Revenue v. Shanghai, Inc.*, IT 02-1 (Office of Admin. Hearings Feb. 7, 2002). If the employer-employee relationship does not exist, any payment for services performed does not constitute “compensation.” *Id.*

Furthermore, for purposes of the 80/20 Test, the payroll fraction measures the compensation that is paid by the entity being analyzed—not compensation paid by some other entity to its employees. 35 Ill. Comp. Stat. 5/304(a)(2)(A); Ill. Admin. Code tit. 86, § 100.3360(a); *see Ill. Dep’t of Revenue v. Shanghai, Inc.*, IT 02-1 (Office of Admin. Hearings Feb. 7, 2002). The Office of Administrative Hearings expressly recognized that the Department is precluded from imputing payroll from one entity to another. *Ill. Dep’t of Revenue v. Shanghai, Inc.*, IT 02-1 (Office of Admin. Hearings Feb. 7, 2002).

Pursuant to Illinois statute, the payroll factor can only measure the compensation paid by WTC to its employees (as defined in Illinois statute and regulation)—not the compensation paid by some other entity (*e.g.*, IBM) to its legal employees. However, the Department disregarded the statutory mandate and imputed compensation from IBM to WTC for the 80/20 Test. *See* Answer ¶¶ 51, 52; Workpapers, Schedules X-2 and X-3.

The Department has not cited—and cannot cite—any legal authority permitting it to impute payroll to WTC for purposes of the 80/20 Test. Such authority does not exist. Pursuant to Illinois statute, the payroll fraction must be calculated in accordance with Illinois tax law and must analyze only the entity in question. Furthermore, the payroll fraction must reflect only

compensation paid to the entity's employees as defined in Illinois statute and regulation.

Therefore, the Department does not have legal authority to impute payroll to WTC for the 80/20 Test.

ii. The Department Does Not Have the Authority to Impute Property to WTC for the 80/20 Test

Illinois tax law mandates that an entity's property fraction is a fraction comprised of a numerator, which is the average value of that entity's 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 that entity's real and tangible personal property owned or rented and used in the trade or business during the taxable year. 35 Ill. Comp. Stat. 5/1501(a)(27)(A); 35 Ill. Comp. Stat. 5/304(a)(1)(A). For purposes of the 80/20 Test, the property fraction measures the value of the property that is owned or rented by the entity being analyzed—not the value of the property that is owned or rented by some other entity. 35 Ill. Comp. Stat. 5/304(a)(1)(A); Ill. Admin. Code tit. 86, § 100.3350(a), (d)-(f); *see Ill. Dep't of Revenue v. Shanghai, Inc.*, IT 02-1 (Office of Admin. Hearings Feb. 7, 2002).

Pursuant to Illinois statute, the property fraction can only measure the value of the property that is owned or rented by WTC—not the value of the property that is owned or rented by some other entity (*e.g.*, IBM). However, the Department disregarded the statutory mandate and imputed property from IBM to WTC for the 80/20 Test. *See* Answer ¶¶ 42-44; Workpapers, Schedules X-1 and X-3.

The Department has not cited—and cannot cite—any legal authority permitting it to impute property to WTC for purposes of the 80/20 Test. Such authority does not exist. Pursuant to Illinois statute, the property fraction must be calculated in accordance with Illinois tax law and can analyze only the entity in question. Therefore, the Department does not have legal authority

to impute property to WTC for the 80/20 Test.

IV. CONCLUSION

For the reasons stated above, IBM respectfully requests this Tribunal find there are no genuine issues of material fact related to the issue of whether the Department has the legal authority to impute payroll and property from one entity to another for purposes of the 80/20 Test and, therefore, that IBM is entitled to judgment as a matter of law. IBM respectfully requests this Tribunal grant IBM's Motion for Summary Judgment and eliminate the Department's Notices.

Respectfully submitted,

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Attorneys for Petitioner

By:



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DATED: March 19, 2015

EXHIBIT A

Sch X-1
A.M. 8/23/12

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)	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. See attached Exhibit 2
- b. IBM World Trade Corporation has 14 executives at Armonk location. (Source: wiki.com getting the info from Dun & Bradstreet- Exhibit 3)

- (1) approx. square feet needed per employee estimate - (Source: www.mbfinancial.sbresources.com) See copy attached Exh. 1
- (2) Number of employees at 1 Orchard Road Armonk, NY location (source: www.manta.com) See copy attached Exhibit 2
- (3) Cost to rent office space in westchester business park, Armonk NY is \$15/sq ft. (Source: www.showcase.com Exhibit 4)

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
- (7) Taxpayers response to one IDR-4 dated July 25, 11. (Enclosed a copy as Exhibit 7)

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 Dat	Resigned D	2007 Salary	2008 Salary
1 Joyce A Bergman (b)	Assistant Secretary	6/30/1989		1,000,000	1,020,000
2 Andrew Bonanzi (b)	Secretary	6/30/1997		500,000	520,000
3 Harsh Chugh (b)	Assistant Treasurer	4/1/2008	11/20/2009		250,000
4 Douglas T. Elix (a) (c)	Chairman, President & CE	5/12/2004	4/1/2008	6,498,370	1,750,000
5 John P. Gianukakis (b)	Controller	9/30/2005	2/2/2010	400,000	415,000
6 Jesse J. Greene (b)	Treasurer	5/10/2002	10/3/2007	600,000	
7 David L. Johnson (b)	VP Corp. Development	4/23/2001	6/11/2009	6,500,000	7,500,000
8 Franklin R. Kern III (b)	Chairman, President & CE	4/1/2008	6/11/2009		6,825,000
9 Martin Schroeter (b)	Assistant Treasurer	6/29/2007	10/3/2007	350,000	
Martin Schroeter	Controller	2/2/2010	4/26/2010		
Martin Schroeter	Treasurer	10/3/2007			400,000
10 Maureen Sladek (b)	VP	11/14/2008			1,250,000
12 Gerard Vilcot (b)	Controller	10/31/1994		750,000	1,000,000
13 Daniel M Zuchelli (b)	Assistant Treasurer	5/23/2005	4/1/2008	400,000	450,000
Total				16,998,370	21,380,000

(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.

(c) Used \$7 million prorated for 3 months. The balance posted to Franklin Kern, Chairman who replaced Elix

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	(*) Promoted 25'	6,282,682	7,135,598
2 Lucio Stanca	President	(b)	6,500,000	7,000,000
3 Greg Watson	Manager			
4 Robin Wilner	Manager			
5 Alan Ganck	V.P.			
6 John Jackson	V.P.			
7 Abby Konstantin	V.P.			
8 Robert Woods	V.P.			
9 Bruce Harreld	General Manager			
10 Grace Suli	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

(*) was derived from IBM Notice of 2008-2009 Annual Meeting & Proxy Statement - 2007 & 2008 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

A.M. 8/23/12

12/31/2007

U.S. F.Assets (state by state)

Property Ratio

	Beginning	Ending	Total	Average
Inv. Dep Assets & Land	752,202	1,672,749	2,424,951	1,212,476
Add cap.rent exp. (1,694,700*8 Sch X-1)		0		13,557,600 (*)
Add Est.cap. leases for Exec & salesmen				1,680,000 (a)
Total U.S. Property	752,202	1,672,749	2,424,951	16,450,076

(*) 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	85,097,853	74,674,101	159,771,954	79,885,977	US 1120 Balance Sheet
Add Cap. Rent Exp. US 1120 Line 16 - 1,507,812				12,062,496	
Add Total Property including Imputed Rent Exp.				16,450,076	
Less: Inv Dep Assets & Land included in U.S. that's included in Everywhere				(1,212,476.00)	
Total Property Everywhere				107,186,073	

U.S. Property percentage

0.153472135

U.S. Payroll

U.S. Payroll Provided by TP (Apportionment data by location)
Add: Salaries & Wages for Officers of WTC & prorated portion of the Chairman of IBM
Total U.S. Imputed Payroll

Version #1 (Includes prorated %age of IBM)
Payroll Ratio

2,049,242
29,781,052 Sch X-2
31,830,294 (x)

Version #2 (without prorating IBM's Officers)
Payroll Ratio

2,049,242
16,998,370
19,047,612

Everywhere Payroll

Total payroll per U.S. 1120 Line 13
Less: U.S. payroll included above on Line 13 of U.S. 1120
Add: Total U.S. Imputed payroll & officers comp.
Grand Total of Payroll Everywhere

Version #1 (Includes prorated %age of IBM)

U.S. 1120 L 1: 30,682,327
See above (2,049,242)
see above (x) 29,781,052
58,414,137

Version #2 (without prorating IBM's Officers)

30,682,327
(2,049,242)
16,998,370
45,631,455

U.S. Payroll percentage

0.544907

0.41742285

U.S. Property percentage from above

0.153472

0.153472

Total of U.S. payroll & U.S. property

0.698379

0.570894985

Average U.S. Ratio

0.3491895

0.285447493

Property Ratio

U.S. F.Assets (state by state)	Beginning	Ending	Total	Average
Inv. Dep Assets & Land	1,672,749		338,379	2,011,128
Add cap.rent exp. (see sch X-1 for detail)		0		1,005,564
Add Est.cap. leases for Exec & salesmen				13,557,600 (*)
Total U.S. Property				1,680,000 (a)
				16,243,164

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	74,674,101	71,491,740	146,165,841	73,082,921 US 1120 B.S.
Add Cap. Rent Exp. US 1120 Line 16 (1,635,880*8)				13,087,040 US Line 16
Add Total U. S. prop. Including imputed amount				16,243,164
Less: Inv Dep Assets & Land included in U.S. that's included in Everywhere				(1,005,564)
Total Property Everywhere				101,407,561

Property Factor: US. Property/Everywhere Property for 80/20 test 0.160177

U.S. Payroll

U.S. Payroll provided by the taxpayer and/or booked on WTC	1,912,319
Add: Sal. & Wages for Officers of WTC & prorated Portion of IBM's Chairman	35,515,598 Sch X-2
Total U.S. Payroll	37,427,917

Version #1 (Includes prorated %age of IBM Version #2 (without prorating IBM's Officers)

Payroll Ratio	Payroll Ratio
1,912,319	1,912,319
35,515,598 Sch X-2	21,380,000 Sch X-2
37,427,917	23,292,319

Everywhere Payroll

Total payroll claimed on U.S. 1120	14,992,484
Less: U.S. payroll included in the above amt.	(1,912,319)
Add: Salaries/wages/compensation from above	35,515,598 Sch X-2
Total Payroll Everywhere	48,595,763

Version #1 (Includes prorated %age of IBM Version #2 (without prorating IBM's Officers)

14,992,484	14,992,484
(1,912,319)	(1,912,319)
35,515,598 Sch X-2	21,380,000 Sch X-2
48,595,763	34,460,165

U.S. Payroll Ratio	0.770189	0.675920
Add: U.S. Property Ratio	0.160177	0.160177
Total U.S. property & payroll Factor	0.930366	0.836097
Average U.S. property	0.465183	0.418049
U.S. property	Greater than 20%	Greater than 20%

EXHIBIT B

Notice of Deficiency

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



#BWNKMGV
#CNXX X173 1727 6328#
INTERNATIONAL BUSINESS MACHINES CORP
ATTN: INCOME TAX DEPT
NORTH CASTLE DRIVE
ARMONK NY 10504

September 24, 2014



Letter ID: CNXXX17317276328

Taxpayer ID: 13-0871985
Reporting period: December 2007
Total Deficiency: \$15,949,669.74
Balance due: \$15,949,669.74

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 "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 this notice. If you file a protest on time, we must reconsider the proposed deficiency, and if requested, grant you or your authorized representative an administrative hearing. An administrative hearing is a formal legal proceeding conducted pursuant to 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 deficiency 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 balance due 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,

Brian Hamer
Director

ILLINOIS DEPARTMENT OF REVENUE
AUDIT BUREAU
PO BOX 19012
SPRINGFIELD IL 62794-9012

(217) 785-4472

Statement

Date: September 24, 2014
Name: INTERNATIONAL BUSINESS MACHINES CORP
Taxpayer ID: 13-0871985
Letter ID: CNXXX17317276328

Reasons for deficiency

See attached Explanation of Adjustments.

If this liability qualified for amnesty, and you did not pay that liability during the amnesty period held October 1, 2010, through November 8, 2010, your penalty and interest amounts may be doubled. [86 Ill. Admin. Code 520/101(b)]

Penalties

We are imposing an additional late-payment 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 additional 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)] (for liabilities due on or after 1/1/2005)

Interest

Interest on tax in the amount of \$3,778,124.34 has been computed through September 24, 2014.

Statement

Date: September 24, 2014
Name: INTERNATIONAL BUSINESS MACHINES CORP
Taxpayer ID: 13-0871985
Letter ID: CNXXX17317276328

Computation of deficiency

Reporting Period: 31-Dec-2007

Income or loss	
Federal taxable income	\$3,834,211,925.00
Net operating loss deduction	\$164,236,410.00
State Municipal and other interest excluded	\$43,077,315.00
Income tax and replacement tax deduction	\$178,436.00
Other additions	\$0.00
Income or loss	\$4,041,704,086.00
Base income or loss	
Foreign dividends subtraction	\$927,869,456.00
Total subtractions	\$927,869,456.00
Base income or net loss	\$3,113,834,630.00
Income allocable to Illinois	
Non-business income or loss	\$0.00
Non-unitary partnership bus. income or loss	\$0.00
Business income or loss	\$3,113,834,630.00
Apportionment formula	
Total sales everywhere	\$34,934,020,174.00
Total Illinois sales	\$1,485,046,920.00
Apportionment factor	0.042510
Business income/loss apportionable to IL	\$132,369,110.00
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	\$132,369,110.00
Net income	
Base income or net loss	\$132,369,110.00
IL net loss deduction (NLD)	\$0.00
Net income	\$132,369,110.00
Net replacement tax	
Replacement tax	\$3,309,228.00
Recapture of investment credits	\$0.00
Replacement tax before credits	\$3,309,228.00
Replacement tax investment credits	\$0.00
Net replacement tax	\$3,309,228.00
Net income tax	
Income tax	\$6,353,717.00
Recapture of investment credits	\$0.00

Statement

Date: September 24, 2014
Name: INTERNATIONAL BUSINESS MACHINES CORP
Taxpayer ID: 13-0871985
Letter ID: CNXXX17317276328

Income tax before credits	\$6,353,717.00
Income tax investment credits	\$0.00
Net income tax	\$6,353,717.00
Refund or balance due	
Net replacement tax	\$3,309,228.00
Net income tax	\$6,353,717.00
Total net income and replacement tax due	\$9,662,945.00
Minus tax previously assessed	-\$968,984.00
Total tax deficiency	\$8,693,961.00
UPIA-5 late-payment penalty (Audit)	\$3,477,584.40
Plus interest on tax through September 24, 2014	\$3,778,124.34
Total deficiency	* \$15,949,669.74

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

Computation of balance due

Remaining amount due (or overpaid)	-\$266.37
Balance due	* \$15,949,403.37

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 that 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 to a credit (or, in some cases, a refund) of that overpayment.
- For more information about these rights and other Department procedures, you may contact us. Our contact information is on the front of this notice.

EXPLANATION OF ADJUSTMENTS

Page 1
07/29/2014

Taxpayer Name: International Business Machine Corp.
FEIN:
Audit Period: 12/31/07 12/31/08

13-0871985

Adjustments

12/31/2007 12/31/2008

We have corrected your IL income tax return to reflect the proper computation using the combined filing method. Ref: IITA Section 1501(a)(27) & 502(e).		4,049,441,572	6,457,284,154
We adjusted the IL net loss deduction since Illinois law requires that losses be recomputed for only the portion attributable to IL on or after 12/31/86. Ref: IITA Sec. 207.			30,606,836
Your NOL add back did not include the NOL amount related to one of your unconsolidated company.			-30,606,836
We have corrected computational errors in the calculation of your Illinois' addition modifications. Ref: IITA Section 1501(a)(12)(A).			30,606,836
We have corrected your addition modifications to reflect the proper computation using the combined filing method. Ref: IITA Section 1501(a)(27) & 502(e).		-454,266,286	-381,974,553
You reported Bonus Depreciation adjustment as net whereas, the Department requires to add back the Federal amount and deduct current dep. as shown on IL-4562.			202,929,413
We have corrected your subtraction modifications to reflect the proper computation using the combined filing method. Ref: IITA Section 1501(a)(27) & 502(e).		794,246,017	4,085,464,133
We have corrected computational errors in the calculation of the sales factor. Ref: IITA Section 304(a)(3)(A).	Everywhere		
	Illinois	34,067,266	-611,106
We have corrected your sales factor to reflect the proper computation using the combined filing method. Ref: IITA Section 1501(a)(27) & 502(e).	Everywhere	730,134,954	1,196,676,127
	Illinois		

Notice of Overpayment Adjustment



September 24, 2014



Letter ID: L0836666336

Account ID: 16229-31968

FEIN: 13-0871985

Reporting Period: December 2009

INTERNATIONAL BUSINESS MACHINES CORP
ATTN: INCOME TAX DEPT
NORTH CASTLE DRIVE
ARMONK NY 10504

We changed the amount of overpayment that you requested be applied to your next year's Illinois estimated tax, or the amount that you requested be refunded to you, because we made an adjustment to your return or you were assessed penalty and interest.

Please review the Account Status Section.

Penalties for any late payment of estimated taxes that might result because we applied this overpayment to another liability, may be avoided by following the instructions below.

If the final estimated payment installment date for next year's estimated taxes has not passed, you must pay back the amount we applied to another liability

- within 30 days of the date of this notice, or
- before the next estimated tax installment due date, whichever is later.

If the final estimated payment installment date for next year's estimated taxes has passed, you must pay back the amount we applied to another liability

- by the original due date of your return, without regard to any extended due date, or
- within 30 days of the date of this notice, whichever is later.

If you disagree with the amount identified or have any questions about the application of your Illinois tax overpayment, call the phone number provided in the Account Status Section.

Note: If you are currently under the protection of the Federal Bankruptcy Court, please contact us and provide the bankruptcy number and the bankruptcy court. The bankruptcy "automatic stay" does not relieve your obligation to file tax returns.

Account Status Section

Total overpayment from: Form IL-1120, Corporation Income and Replacement Tax Return \$4,764,335.78

Amount offset to the following:	Phone number	
Total offset amount:		\$0.00
Previous amount of credit carryforward:		\$0.00
Remaining overpayment:		\$4,764,335.78
Amount applied to 12/10 estimated payments	1 800 732-8866	\$4,764,335.78
Refund amount		\$0.00

Note: You will not receive a refund check if your refund amount is less than \$1.

Notice of Overpayment Adjustment



September 24, 2014



Letter ID: L1359621856

Account ID: 16229-31968

FEIN: 13-0871985

Reporting Period: December 2010

INTERNATIONAL BUSINESS MACHINES CORP
ATTN: INCOME TAX DEPT
NORTH CASTLE DRIVE
ARMONK NY 10504

We changed the amount of overpayment that you requested be applied to your next year's Illinois estimated tax, or the amount that you requested be refunded to you, because we made an adjustment to your return or you were assessed penalty and interest.

Please review the Account Status Section.

Penalties for any late payment of estimated taxes that might result because we applied this overpayment to another liability, may be avoided by following the instructions below.

If the final estimated payment installment date for next year's estimated taxes has not passed, you must pay back the amount we applied to another liability

- within 30 days of the date of this notice, or
- before the next estimated tax installment due date, whichever is later.

If the final estimated payment installment date for next year's estimated taxes has passed, you must pay back the amount we applied to another liability

- by the original due date of your return, without regard to any extended due date, or
- within 30 days of the date of this notice, whichever is later.

If you disagree with the amount identified or have any questions about the application of your Illinois tax overpayment, call the phone number provided in the Account Status Section.

Note: If you are currently under the protection of the Federal Bankruptcy Court, please contact us and provide the bankruptcy number and the bankruptcy court. The bankruptcy "automatic stay" does not relieve your obligation to file tax returns.

Account Status Section

Total overpayment from: Form IL-1120, Corporation Income and Replacement Tax Return		\$22,892.78
Amount offset to the following:	Phone number	
Total offset amount:		\$0.00
Previous amount of credit carryforward:		\$0.00
Remaining overpayment:		\$22,892.78
Amount applied to 12/11 estimated payments	1 800 732-8866	\$22,892.78
Refund amount .		\$0.00

Note: You will not receive a refund check if your refund amount is less than \$1.

Taxpayer Statement



September 25, 2014 TDD: 1 800 544-5304



Letter ID: CNXXX13183411362

Account ID: 16229-31968
FEIN: 13-0871985

#BWNKMGV
#CNXX X131 8341 1362#
INTERNATIONAL BUSINESS MACHINES CORP
ATTN: INCOME TAX DEPT
NORTH CASTLE DRIVE
ARMONK NY 10504

This statement lists our most recent information about your unpaid balance, available credits, or returns you have not filed.

IL Business Income Tax You have available credits of \$25,182.06 Account ID: 16229-31968

Period	Tax	Penalty	Interest	Other	Payments/Credits	Balance
31-Dec-2011	15,359,731.00	10,297.87	-	-	(15,395,210.93)	(25,182.06)
31-Dec-2012	24,846,300.00	628,561.81	10,011.49	-	(24,390,090.85)	Not Included*

* We have received correspondence for this period and it is currently under review.

SOA

P-000189

If necessary, respond to:
ILLINOIS DEPARTMENT OF REVENUE
PO BOX 19004
SPRINGFIELD IL 62794-9004

Notice of Deficiency

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



#BWNKMGV
#CNXX X152 9565 7121#
INTERNATIONAL BUSINESS MACHINES CORP
ATTN: INCOME TAX DEPT
NORTH CASTLE DRIVE
ARMONK NY 10504

September 24, 2014



Letter ID: CNXXX15295657121

Taxpayer ID: 13-0871985
Reporting period: December 2008
Total Deficiency: \$11,972,596.94
Balance due: \$11,972,596.94

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 "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 this notice. If you file a protest on time, we must reconsider the proposed deficiency, and if requested, grant you or your authorized representative an administrative hearing. An administrative hearing is a formal legal proceeding conducted pursuant to 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 deficiency 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 balance due 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,

Brian Hamer
Director

ILLINOIS DEPARTMENT OF REVENUE
AUDIT BUREAU
PO BOX 19012
SPRINGFIELD IL 62794-9012

(217) 785-4472

Statement

Date: September 24, 2014
Name: INTERNATIONAL BUSINESS MACHINES CORP
Taxpayer ID: 13-0871985
Letter ID: CNXXX15295657121

Reasons for deficiency

See attached Explanation of Adjustments.

If this liability qualified for amnesty, and you did not pay that liability during the amnesty period held October 1, 2010, through November 8, 2010, your penalty and interest amounts may be doubled. [86 Ill. Admin. Code 520/101(b)]

Penalties

We are imposing an additional late-payment 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 additional 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)] (for liabilities due on or after 1/1/2005)

Interest

Interest on tax in the amount of \$2,246,263.54 has been computed through September 24, 2014.

Statement

Date: September 24, 2014
Name: INTERNATIONAL BUSINESS MACHINES CORP
Taxpayer ID: 13-0871985
Letter ID: CNXXX15295657121

Computation of deficiency

Reporting Period: 31-Dec-2008

Income or loss	
Federal taxable income	\$9,437,765,868.00
Net operating loss deduction	\$160,891,249.00
State Municipal and other interest excluded	\$9,882,623.00
Income tax and replacement tax deduction	\$5,303,711.00
Illinois bonus depreciation addition	\$1,091,981,552.00
Other additions	\$0.00
Income or loss	\$10,705,825,003.00
Base income or loss	
Foreign dividends subtraction	\$6,633,979,077.00
Illinois bonus depreciation subtraction	\$214,021,623.00
Total subtractions	\$6,848,000,700.00
Base income or net loss	\$3,857,824,303.00
Income allocable to Illinois	
Non-business income or loss	\$0.00
Non-unitary partnership bus. income or loss	\$0.00
Business income or loss	\$3,857,824,303.00
Apportionment formula	
Total sales everywhere	\$35,052,333,144.00
Total Illinois sales	\$1,540,893,009.00
Apportionment factor	0.043960
Business income/loss apportionable to IL	\$169,589,956.00
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	\$169,589,956.00
Net income	
Base income or net loss	\$169,589,956.00
IL net loss deduction (NLD)	\$0.00
Net income	\$169,589,956.00
Net replacement tax	
Replacement tax	\$4,239,749.00
Recapture of investment credits	\$0.00
Replacement tax before credits	\$4,239,749.00
Replacement tax investment credits	\$0.00
Net replacement tax	\$4,239,749.00
Net income tax	

Statement

Date: September 24, 2014
Name: INTERNATIONAL BUSINESS MACHINES CORP
Taxpayer ID: 13-0871985
Letter ID: CNXXX15295657121

Income tax	\$8,140,318.00
Recapture of investment credits	\$0.00
Income tax before credits	\$8,140,318.00
Income tax investment credits	\$69,541.00
Net income tax	\$8,070,777.00
Refund or balance due	
Net replacement tax	\$4,239,749.00
Net income tax	\$8,070,777.00
Total net income and replacement tax due	\$12,310,526.00
Minus tax previously assessed	-\$5,363,145.00
Total tax deficiency	\$6,947,381.00
UPIA-5 late-payment penalty (Audit)	\$2,778,952.40
Plus interest on tax through September 24, 2014	\$2,246,263.54
Total deficiency	* \$11,972,596.94

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

Computation of balance due

Remaining amount due (or overpaid)	-\$500.00
Balance due	* \$11,972,096.94

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 that 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 to a credit (or, in some cases, a refund) of that overpayment.
- For more information about these rights and other Department procedures, you may contact us. Our contact information is on the front of this notice.

EXPLANATION OF ADJUSTMENTS

Page 1
07/29/2014

Taxpayer Name: International Business Machine Corp.
FSIN:
Audit Period: 12/31/07 12/31/08

13-0871985

Adjustments	12/31/2007	12/31/2008
We have corrected your IL income tax return to reflect the proper computation using the combined filing method. Ref: IITA Section 1501(a)(27) & 502(e).	4,049,441,672	6,457,284,154
We adjusted the IL net loss deduction since Illinois law requires that losses be recomputed for only the portion attributable to IL on or after 12/31/86. Ref: IITA Sec. 207.		30,606,836
Your NOL add back did not include the NOL amount related to one one of your unconsolidated company.		-30,606,836
We have corrected computational errors in the calculation of your Illinois' addition modifications. Ref: IITA Section 1501(a)(12)(A).		30,606,836
We have corrected your addition modifications to reflect the proper computation using the combined filing method. Ref: IITA Section 1501(a)(27) & 502(e).	-454,266,286	-381,974,553
You reported Bonus Depreciation adjustment as net whereas, the Department requires to add back the Federal amount and deduct current dep. as shown on IL-4562.		202,929,413
We have corrected your subtraction modifications to reflect the proper computation using the combined filing method. Ref: IITA Section 1501(a)(27) & 502(e).	794,246,017	4,085,484,133
We have corrected computational errors in the calculation of the sales factor. Ref: IITA Section 304(a)(3)(A).	Everywhere Illinois	34,067,266 -611,106
We have corrected your sales factor to reflect the proper computation using the combined filing method. Ref: IITA Section 1501(a)(27) & 502(e).	Everywhere Illinois	730,134,954 1,196,676,127

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Respectfully submitted,

SUTHERLAND ASBILL & BRENNAN LLP
Attorneys for Petitioner

By:



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ARDC #6315874

DATED: March 19, 2015