

ILLINOIS INDEPENDENT TAX TRIBUNAL

INTERNATIONAL BUSINESS)	
MACHINES CORPORATION,)	
Petitioner,)	
)	
v.)	14 TT 229
)	Chief Judge James M. Conway
ILLINOIS DEPARTMENT OF REVENUE,)	
Respondent.)	

DEPARTMENT’S MOTION TO COMPEL

NOW COMES the Department of Revenue (“Department”), by its duly authorized representatives, Special Assistant Attorneys General, pursuant to Illinois Supreme Court Rules 213 and 214, moves this Tribunal to enter an order compelling International Business Machines (“IBM” or “Petitioner”) to fully respond to the Department’s First Set of Interrogatories and First Request for Production of Documents, and in support thereof states as follows:

A. Background.

1. IBM and subsidiaries filed Illinois Corporation Income and Replacement Tax Returns (“IL-1120-X”) for tax year ending December 31, 2007 through December 31, 2008 (the “Years at Issue”) claiming an exemption from tax for its subsidiary IBM World Trade Corporation (“WTC”) based on the 80/20 business activity test in Section 1501(a)(27) of the Illinois Income Tax Act (“ITA”).
2. The Department conducted an audit of IBM and its subsidiaries for the Years at Issue.
3. Based on the facts obtained during the audit, the Department’s auditor determined that WTC did not meet the 80/20 business activity test during the Years at Issue.

4. Based on the auditor's determination, the Department issued IBM Notices of Deficiency dated September 24, 2014, for the Years at Issue.

5. On December 2, 2014, this Tribunal received IBM's protest Petition in response to the Notices of Deficiency. The Department filed its Answer on January 7, 2015.

6. At the initial status conference on January 20, 2015, this Tribunal ordered the parties to issue written discovery by March 20, 2015.

7. On March 19, 2015, IBM filed a Motion for Summary Judgment and requested an extension of the time to issue written discovery. This Tribunal's March 19, 2015 Order granted an extension of time to issue written discovery.

8. On March 31, 2015, this Tribunal set a briefing schedule on Petitioner's Motion for Summary Judgment and ordered the parties to file written discovery by April 22, 2015.

9. The parties timely filed the Response and Reply to IBM's Motion for Summary Judgment.

10. On June 30, 2015, this Tribunal denied IBM's Motion for Summary Judgment.

11. In its Order denying Summary Judgment, this Tribunal held that the Department has the authority to determine the correct payroll and property tax figures for WTC. This Tribunal further held that: "Whether IBM was correct in treating WTC as an exempt 80/20 company or whether the Department was correct in denying the exemption cannot be determined until a factual record concerning WTC's U.S and worldwide business activities is developed."

12. On April 22, 2015, the Parties issued discovery.

13. The Parties agreed to an extension of the time for responding of discovery to June 24, 2015. The parties timely tendered discovery responses. A copy of Petitioner's Answers to

Department's First Set of Interrogatories and Petitioner's Written Response to Department's First Request for Production of Documents is attached hereto as Exhibit 1.

14. On July 30, 2015, the parties met via teleconference to discuss the deficiencies in the discovery responses.

15. On August 6, 2015, the parties again conferred by teleconference to try to resolve their discovery disputes.

16. On August 12, 2015, Petitioner's counsel sent Department's counsel a draft Motion for Protective Order and Proposed Protective Order.

17. The parties negotiated an agreed protective order, which the Tribunal entered on September 28, 2015.

18. On October 2, 2015, Petitioner served the Department with Petitioner's Supplemental Responses to the Department's First Set of Interrogatories and Requests for Production of Documents. A copy of Petitioner's Supplement discovery responses is attached hereto as Exhibit 2.

19. Department's counsel promptly reviewed the Petitioner's Supplemental Answers and Production.

20. Pursuant to Illinois Supreme Court Rule 201(k), Department's counsel sent Petitioner's counsel a letter on October 22, 2015, detailing the deficiencies with Petitioner's Answers to Department's First Set of Interrogatories and Petitioner's Production in response to Department's First Request for Production of Documents. A copy of that 201(k) Letter is attached as Exhibit 3.

21. In its letter, Department's counsel asked Petitioner's counsel to contact Department's counsel to discuss the deficient discovery.

22. To date, Petitioner's counsel has not contacted the Department, nor has it produced any additional discovery materials in response to the 201(k) Letter.

B. Issue

23. Department is entitled to full disclosure of discoverable information. Ill. Sup. Ct. R. 201(b)(1) ("Except as provided in these rules, a party may obtain by discovery full disclosure regarding any matter relevant to the subject matter involved in the pending action, whether it relates to the claim or defense of the party seeking disclosure or of any other party, including the existence, description, nature, custody, condition, and location of any documents or tangible things, and the identity and location of persons having knowledge of relevant facts.").

24. The Department asserts that many of Petitioner's responses to the Department's First Set of Interrogatories and First Request for Production of Documents (hereafter "Department's Discovery Requests") are deficient. Accordingly, the Department now Moves to Compel Petitioner's complete responses to the Department's Discovery Requests.

25. The issue in this case is whether IBM can show by clear and convincing evidence that WTC meets the 80/20 business activity exemption. 35 ILCS 5/1501(a)(27) (The unitary business "group will not include those members whose business activity outside the United States is 80% or more of any such member's total business activity."). That is, whether 80% or more of WTC's property and payroll activities were conducted outside the water's edge of the United States.

26. Accordingly, the Department propounded Department's Discovery Requests to obtain facts to determine what evidence exists that would show that WTC meets the 80/20 business activity test.

27. "It is well established that discovery is to be 'a mechanism for the ascertainment

of truth, for the purpose of promoting either a fair settlement or a fair trial.' To this end, the object of all discovery procedures is disclosure, *** however, that right is limited to disclosure regarding matters relevant to the subject matter of the pending action. Nevertheless, great latitude is allowed in the scope of discovery." *Pemberton v. Tieman*, 117 Ill.App.3d 502, 504 (1st Dist. 1983) (Internal citations omitted).

28. In Illinois, the concept of relevance for purposes of discovery is broader than for purposes of admitting evidence at trial. *Id.*; *Bauter v. Reding*, 68 Ill. App. 3d 171, 175 (3d. Dist. 1979).

29. Relevance for discovery purposes includes not only what is admissible at trial, but also that which leads to admissible trial evidence. *TTX Co. v. Whitley*, 295 Ill. App. 3d 548, 556 (1st Dist. 1998); *Pemberton*, 117 Ill.App.3d at 505; *Crnkovich v. Almeida*, 261 Ill. App. 3d 997, 999 (3rd Dist. 1994); *United Nuclear Corp. v. Energy Conversion Devices, Inc.*, 110 Ill. App. 3d 88, 104 (1st Dist. 1982). Therefore, inquiries made under either Rule 213 or Rule 214 are permissible if they seek information that "may" lead to admissible evidence, as opposed to "must" lead to admissible evidence. *TTX Co. v. Whitley*, 295 Ill. App. 3d at 556.

30. "Relevancy is determined by reference to the issues, for generally, something is relevant if it tends to prove or disprove something in issue." *Bauter v. Reding*, 68 Ill. App. 3d at 175.

31. In the instant matter, the Department requested information pertaining to the real and tangible personal property and payroll of WTC. Additionally, Department requested information to identify what person(s) performed these activities on behalf of WTC. Accordingly, the Department's Discovery Requests are relevant to the 80/20 exemption claimed by Petitioner.

32. Inasmuch as the Department's Discovery Requests seek information regarding the real and tangible personal property owned, leased or used by WTC, the compensation for services performed by employees of WTC, and the activities performed on behalf of WTC, Petitioner's relevance objections are not valid, and therefore must be overruled. *Zebra Technologies Corp. v. Topinka*, 344 Ill.App.3d 474, 482-483 (1st Dist. 2003) (The foreign subsidiaries "had other individuals in the U.S. performing activities for these companies." "Zebra knew the amount of time spent by the committee on quality control issues and was capable of allocating this expense to the Bermuda companies because it was this committee which was protecting the license for these companies.").

33. Petitioner objected to several of Department's Discovery Requests on the basis that the information sought was protected by the attorney-client privilege. Interrogatory Response No. 12 and Document Responses No. 1, 2, 24, 27, and 32. Petitioner has not tendered a privilege log or otherwise supported its privilege claim "with a description of the nature of the documents, communications or things not produced or disclosed." Ill. Sup. Ct. R. 201(n). Department requests the Tribunal overrule Petitioner's objections and order Petitioner to provide a response to Interrogatory No. 12 and all responsive documents to Production Requests No. 1, 2, 24, 27, and 32.

C. **Interrogatories** (To prevent confusion, Department has referred to each discovery request by its number, and has not otherwise numbered the following paragraphs.)

Interrogatory No. 3. Interrogatory 3 requests "the names,... job titles, job descriptions, and work addresses of the individuals that comprise the [REDACTED] [REDACTED] of wages paid by WTC to IBM under the Shared Services Cost Sharing Amendments." In its response to Interrogatory No. 3, Petitioner objected asserting the interrogatory "as overbroad and vague as to what the Department means by "wages paid by WTC to IBM."

Petitioner further answered that “WTC did not pay to IBM wages.” However, the language objected to in Interrogatory No. 3 is taken from the Department’s June 25, 2014 Informal Conference Board (“ICB”) Action Decision (“6/25/14 ICB Action Decision”), which Petitioner referenced in its Petition. Petition, ¶¶58, 59. Petitioner completely understood the phrase “wages paid by WTC to IBM” in the 6/25/14 ICB Action Decision when it referenced the Action Decision in its petition. Specifically in paragraphs 58 and 59 of its Petition, Petitioner alleged that the 6/25/15 ICB Action Decision “expressly held that the Department could not impute research and development payroll to WTC from the cost share payment to IBM for purposes of the 80/20 test.” Petition, ¶59.

The requested Interrogatory No. 3 solicits information regarding the cost share payment by WTC to IBM. This cost share payment comprised wages paid by IBM to its employees for Research and Development (“R&D”) expenses, Brand Headquarter (“BHQ”) expenses and Corporate Headquarter (“CHQ”) expenses. IBM_0094, 0132, 0152. (All of the IBM bates documents referenced herein are attached as Exhibit 4, which is filed under seal.) R&D expenses include [REDACTED]

[REDACTED]

[REDACTED] [REDACTED]

[REDACTED]

[REDACTED]

[REDACTED] BHQ and CHQ expenses are [REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]
[REDACTED]
[REDACTED]
[REDACTED] and

CHQ expense includes [REDACTED]
[REDACTED]
[REDACTED]
[REDACTED]
[REDACTED]

[REDACTED] IBM_0094, 0132, 0152. Department believes these activities are performed by IBM employees. However, these activities benefit WTC in that WTC does not have to have its own employees to perform R&D, IP protection, H/R, legal services, etc. But the question remains, what amount does WTC reimburse IBM for these activities? Petitioner disputes the amounts listed in the 6/25/15 Action Decision as wages, [REDACTED] [REDACTED] which are almost 40 times higher in 2007 and 80 times higher in 2008 than the amount of WTC everywhere payroll as alleged by Petitioner in its Petition - [REDACTED]

It is wholly within the Department's rights to inquire into the U.S. business activities directly related to the intellectual property that comprises most, if not all, of WTC's revenues. Whether the amount of wages in the 6/25/15 ICB Action Decision are exact does not abrogate Petitioner's duty to properly respond to this interrogatory. Moreover, the Department has the right to discover facts that may lead to relevant information regarding the "substance over form" of the transactions between IBM and WTC. The amount WTC paid to IBM for activities that

generated WTC's income for the periods are relevant to the business activities of WTC for purposes of the 80/20 business activity test. *Zebra Technologies Corp. v. Topinka*, 344 Ill.App.3d 474, 484 (1st Dist. 2003).

Interrogatory No. 4. This interrogatory requests that Petitioner provide the job title, duties/job description, work location (address, city, state, zip code) of each WTC U.S. employee and provide the name of each person who had authority to direct the manner of each employee's performance of work, including hiring and termination of employment for each employee of WTC. Petitioner answers this interrogatory by referencing Bates number IBM_0001 and IBM_0234 through IBM_0265. However, those documents do not fully answer the interrogatory asked, namely, the documents do not provide the work location(s) (address, city, state, zip code), or the name and position of each person who had authority to direct the employee's work. In its petition, Petitioner references these employees (¶96). Additionally, the activities of these employees are at the heart of the Business Activity test. Department requests the Tribunal overrule Petitioner's objections and order Petitioner to provide the requested information.

Interrogatory No. 5. In Interrogatory No. 5, the Department seeks each real property location (address, city and state) in the United States where an officer, director, employee or agent of WTC performed services, including training, on behalf of WTC.

In its response to Interrogatory No. 5, Petitioner objected asserting that the request is oppressive, unduly burdensome irrelevant and beyond the scope of discovery. Petitioner also objected and stated that the interrogatory sought information outside its possession, knowledge or control. Petitioner objected to the interrogatory claiming it was overbroad and vague. Petitioner lastly objected to the interrogatory and claimed that it was improper because it sought an admission of law or requires a legal conclusion with respect to determining who is an "agent"

to WTC and what it means to perform services "on behalf of WTC." In Petitioner's First Supplemental Response to the Department's First Set of Interrogatories, Petitioner identified W-2 Forms (Bates numbers IBM_0195 through IBM_0233) as responsive. While these documents identify the names of the WTC officers and IBM's location for payroll purposes, the documents do not "state the address, city and state of each real property location in the United States..." as the Department requested in Interrogatory 5. Petitioner has not identified the U.S. work location(s) (address, city, state) of any WTC director, officer or employee. Additionally, Petitioner did not identify the locations where agents of WTC performed services on behalf of WTC.

Petitioner's objections should be overruled. First, the term "agent" is defined on page 4 of Department's First Set of Interrogatories (Definition Paragraph 22.). Second, the information sought is relevant. To determine whether 80% or more of WTC's business activities are performed outside the United States, requires a determination of the property factor which includes both tangible personal property and real property. The location of real property is essential to determining whether or not property is within the water's edge of the United States. Additionally, the location can be used to determine the value of that property. Real property includes office buildings, storage facilities, cafeterias, parking lots, parking garages, health/exercise facilities, conference facilities, training facilities, etc. Third, Petitioner should know where WTC's employees, officers and directors worked and where the agents thereof performed services. Department requests the Tribunal overrule Petitioner's objections and order Petitioner to provide the requested information.

Interrogatory No. 6. The Department, in Interrogatory No. 6, asked for the location of real property (address, city and state) where an officer, director, employee or agent of

Petitioner/IBM performed services on behalf of WTC. In its response to Interrogatory No. 6 Petitioner objected asserting that the request is oppressive, unduly burdensome irrelevant and beyond the scope of discovery. Petitioner also objected and stated that the interrogatory sought information outside its possession, knowledge or control. Petitioner objected to the interrogatory claiming it was overbroad and vague. Petitioner lastly objected to the interrogatory and claimed that it was improper because it sought an admission of law or requires a legal conclusion with respect to determining who is an "agent" of Petitioner/IBM and what it means to perform services "on behalf of WTC."

Petitioner's objections should be overruled. "Agent" is defined in Paragraph 22 of the Definitions section on Page 4 of the Interrogatories. Additionally, the Department, in determining what business activity IBM is performing on behalf of WTC, has the right to evaluate information relating to real property used in performing services by or on behalf of WTC. In making this determination, the Department is entitled to discover all property factors, which includes of the location of real properties including, but not limited to, offices, storage facilities, cafeterias, parking lots, health/exercise facilities, conference rooms, lobbies, training facilities, etc. Petitioner should know where employees and officers perform services for itself and its wholly owned subsidiary. Department requests the Tribunal overrule Petitioner's objections and order Petitioner to provide the requested information.

Interrogatory No. 7 requests "the cost, lease amount or fair market value (as applicable) for all items of tangible personal property used by any officer, director, employee, or agent of WTC in performing services on behalf of WTC in the United States, including territories." The Department also identified a non exhaustive list of examples of tangible personal property.

In its response to Interrogatory No. 7, Petitioner objected to the request as oppressive and unduly burdensome, and that the information sought was outside its possession, knowledge or control. Petitioner claimed the term "performing services on behalf of WTC" is vague and over broad. Petitioner also claimed the interrogatory seeks an admission of law or requires a legal conclusion. Petitioner further claims that the information sought in this interrogatory is already in the Department's possession.

Petitioner's objections should be overruled because the Department, in determining whether more than 80% of WTC's business activities are operated or conducted outside the United States, has the right to examine the value of tangible personal property WTC used in the United States.

Petitioner's First Supplemental Response to the Department's First Set of Interrogatories identified documents Bates numbers IBM_0308 through IBM_0341 as responsive. These documents contain beginning and ending balances for tangible property owned by WTC for 2007 and 2008. Petitioner also provided a schedule of Rent Expense showing ending rent expense for real and personal property. However, Petitioner has failed to provide the cost or fair market value of the tangible personal property. Rather Petitioner has provided only the book value "total" for tangible property. Book value represents the value of the assets after depreciation for both prior and current years. Petitioner has not provided the cost for the owned property. According to Regulation 100.3350(e), "Property owned by the person shall be valued at its original cost. As a general rule "original cost" is the basis of property for federal income tax purposes at the time of acquisition and will not reflect any federal adjustments thereafter for deductions for depreciation, depletion, amortization and the like." 86 Ill. Admin. Code 100.3360(e). Section (f) of the Regulation provides for the valuation of leased property as

follows:

Property rented by the person is valued at eight times the net annual rental rate. The net annual rental rate for any item of rented property is the annual rental rate paid by the person for such property, less the aggregate annual subrental rates paid by subtenants of the person. (See Section 100.3380(a) for special rules where the use of such net annual rental rate produces a negative or clearly inaccurate value or where property is used by the person at no charge or rented at a nominal rental rate.) Subrents are not deducted when the subrents constitute business income because the property which produces the subrents is used in the regular course of a trade or business of the person when it is producing such income. Accordingly there is no reduction in its value.

86 Ill. Admin. Code 100.3350(f). Petitioner's Rent Expense schedule shows that it does not pay rent for the use of tangible property in the United States. However, the special rules in Regulation 100.3380 provide: "If property owned by others is used by the person at no charge or rented by the person for a nominal rate, the net annual rental rate for the property shall be determined on the basis of a reasonable market rental rate for such property." 86 Ill. Admin. Code 100.3380(b)(2). Thus, Petitioner should also identify the items of tangible personal property used by an officer, director, employee, or agent of WTC in performing services on behalf of WTC in the United States, including territories, for which WTC does not pay a fee. The identification should be specific enough for the Department to determine "a reasonable market rental rate for such property."

Department requests the Tribunal overrule Petitioner's objections and order Petitioner to provide the missing information.

Interrogatory No. 8 requests "the cost, lease amount or fair market value (as applicable) for all items of tangible personal property used by any officer, director, employee, or agent of IBM in performing services as described in The Shared Services Cost Sharing Amendments on behalf of WTC in the United States, including territories."

Petitioner objected and stated the request was irrelevant and beyond the scope of discovery that it is oppressive and unduly burdensome. Petitioner also claimed that the Department's interrogatory seeks information outside its knowledge, possession or control. Petitioner claimed the term "performed services on behalf of WTC" is vague. Petitioner also objected claiming the interrogatory required an admission of law or a legal conclusion in determining who is an "agent" of IBM and what it means to perform services "on behalf of WTC." "Agent" is defined in Paragraph 22 of the Definitions section on Page 4 of the Interrogatories.

Again, Department seeks this information pursuant to Regulations 100.3350 and 100.3380. Those regulations provide that for purposes of the property factor, owned property be valued at cost, leased property be valued at eight times its net annual rental rate, and property which is used at no charge be valued at reasonable market rental rate. Department requests the Tribunal overrule Petitioner's objections and order Petitioner to provide the missing information.

Interrogatory No. 9 seeks a description of WTC's business purpose, including how WTC fits into IBM's business model, the types of goods sold by WTC, the services provided by WTC, vendors and suppliers of WTC, customers of WTC, and the means or processes by which WTC sells the goods or services described. The purpose of this Interrogatory is to gain a better understanding of WTC's business – what it does, how it does it, and who it does it for. Petitioner objected to Interrogatory 9 on that basis that it was "oppressive and unduly burdensome" to name WTC's vendors and suppliers and customers. Petitioner must demonstrate how this request is "oppressive and unduly burdensome." Ill. Sup. Ct. R. 201(c)(3). Petitioner objected that "business purpose" and "means and processes" are "overbroad and vague."

The only responsive information taxpayer provided was that "WTC receives royalties

from controlled foreign corporations (“CFCs”) related to the sale of hardware, software and services outside the United States,” and that “WTC operated a network of foreign branches that ... performed sales distribution functions including sales, finance, human resources, marketing, sales operations, delivery and customer service.” However, this statement did not answer the entire Interrogatory posed. Is WTC the seller of the hardware, software and services to the CFCs? If not, what does it do to receive royalty income? If WTC sells hardware, software, and services, where is the hardware manufactured? Where is the software designed? And where are the services performed? Does WTC own the intellectual property for the hardware, software and services it sells? Who are the CFCs? Are they owned by IBM or WTC? What does WTC do to earn royalty income? What is the selling process? Department requests this Tribunal overrule Petitioner's objections, order the Petitioner to provide a more detailed response to Interrogatory 9 and order Petitioner to identify the person providing this response so that Department may later depose this person.

Interrogatory No. 10 seeks “the address, city and state and country” where inventory was stored. Petitioner objected that Interrogatory 10 is “overbroad and vague,” “irrelevant and beyond the scope of discovery.” Inventory is tangible personal property. The place of storage is real property. Therefore, the location (and value) of inventory storage facilities is relevant to the property factor of the 80/20 business activity test. Petitioner responded that “the vast majority of any inventory owned by WTC was outside the U.S. during the Tax Years at Issue.” Petitioner provided a summary document showing the value of inventory by state for 2007 and 2008, respectively. In Petitioner's First Supplemental Response to the Department's First Set of Interrogatories, Petitioner provided the same documents. However, these documents do not provide the address, city or, for foreign facilities, the country where inventory is stored. The

documents only show the state and "foreign" totals for inventory. Department requires the address, city and state of the storage facility to acquire more detailed information regarding the facility – the legal owner, the real estate value, the rent or lease payments for use of the facility, etc. Department requests this Tribunal overrule Petitioner's objections, order the Petitioner to provide the street address, city, state, and country of each facility where WTC stored inventory during the years at issue.

Interrogatory No. 11. The Department has the right to discover the specifics of WTC's domestic and foreign property and payroll. This interrogatory asks for a list of WTC locations, activities, employees, job descriptions, and salaries. These are all relevant to verifying numerous allegations regarding property and payroll in Petitioner's petition that Petitioner itself put at issue in this matter. In its Supplemental Response to the Department's First Set of Interrogatories dated October 2, 2015, Petitioner referenced and produced documents numbered IBM_0234, and IBM_0266 through IBM_0280 as completely responsive to the interrogatory. With regard to the domestic employees of WTC, the documents do not fully answer the interrogatory asked, namely, the address of the work location (street address, city, state, zip code) of each employee. Regarding the foreign employees, while the supplemental response includes the names and job titles, there are no job descriptions/duties, salaries or activities provided. Therefore, the response is incomplete. Additionally, Petitioner did not "describe the activities of each division." Department requests the Tribunal overrule Petitioner's objections and order Petitioner to provide the missing information.

Interrogatory No. 12. In Interrogatory 12, the Department asks Petitioner to identify each person that performed the delineated activities for WTC. Those activities are:

- a. **Solicitation of prospective customers;**
- b. **Place where purchase orders are received;**
- c. **Finalizing and signing the final agreement (i.e. sales contract, license, etc);**
- d. **Financing, credit check and approval;**
- e. **Preparation of customers' account information (including account statements, sales invoices);**
- f. **Preparing, packing, carting, and shipping products to customers, and;**
- g. **Maintenance of accounting services (including account receivables/payables and preparation of financial statements and tax forms (including Form 1120 and its source documentation)).**

Instead of answering the interrogatory, Petitioner provided a narrative and listed work categories (“sales distribution functions, including sales, finance, human resources, marketing, sales operations, delivery, and customer service”) performed by WTC foreign employees. The narrative is wholly unresponsive to the interrogatory. In its Supplemental Response to the Department’s First Set of Interrogatories dated October 2, 2015, Petitioner referenced and produced documents numbered IBM_234, and IBM_0266 through IBM_0280 as completely responsive to the interrogatory. Again, these documents list the name of the employee, the country and an abbreviation of the employee’s job title. Supreme Court Rule 213(e) allows for the production of documents instead of a written response to the interrogatory posed, but only “when the answer to an interrogatory may be obtained from documents in the possession or control of the party on whom the interrogatory was served.” Ill. Sup. Ct. R. 213(e). Here, the documents do not provide the person(s) who performed the defined activities. Department requests the Tribunal overrule Petitioner’s objections and order Petitioner to provide a complete Answer.

Interrogatory No. 13. In Interrogatory 13, Department asked Petitioner to “Identify the real property and tangible personal property (by manufacturer, model number and date placed in service) WTC owned, leased or used during the Tax Years at Issue and state the location of that property (street address, city, state and country).” Petitioner objected that the interrogatory was

“duplicative,” “oppressive and unduly burdensome,” and “seeks information outside the Petitioner’s possession, knowledge, or control.” Petitioner did not provide any response to Interrogatory 13. Petitioner must demonstrate how this request is “oppressive and unduly burdensome.” Additionally, the explanatory Committee Comments to Illinois Supreme Court Rule 214 provides that a party must fully disclose the party's knowledge of the existence and location of responsive documents, objects or tangible things not in its possession so as to enable the requesting party to obtain the responsive documents, objects or tangible things from the custodian. Ill. Sup. Ct. R. 214, Committee Comments.

Documents produced by Petitioner (IBM 0025 and 0029) in response to other requests show WTC paid \$0 of U.S. rent expense and WTC owned \$0 real property (IBM 0020 and 0027) in the U.S. Yet, [REDACTED] of inventory in New York. IBM_0015. Additionally Petitioner admits that WTC had 20 employees in New York in 2007 and 2008, respectively. Therefore, Department has reason to believe that WTC employees and agents used both tangible personal property and real property in the course of WTC’s trade or business that WTC did not own and for which WTC did not rent (or otherwise pay a fee to use). Pursuant to Regulation 100.3380(b)(2), the property factor includes all property “if it is actually used or is available for or capable of being used during the tax period in the regular course of the trade or business of the person.” 86 Ill. Admin. Code 100.3350(b). The value of that property for purposes of the property factor is its original cost, if owned, or eight times the net annual rental rate, if leased. 86 Ill. Admin. Code 100.3350(e) and (f). However, “[i]f property owned by others is used by the person at no charge or rented by the person for a nominal rate, the net annual rental rate for the property shall be determined on the basis of a reasonable market rental rate for such property.” 86 Ill. Admin. § Code 100.3380(b)(2). Property

used by WTC that was not owned or leased is not included in the state summary schedules Petitioner provided (IBM_0003 to_0029). Additionally, the state summary schedules (IBM_0003 to_0029) do not identify any property (by address, or manufacturer, model number and date placed in service), only the value of undisclosed property. Department requests this Tribunal overrule Petitioner's objections, and order the Petitioner to provide a full response to Interrogatory 13.

Interrogatory No. 14. In Interrogatory 14, Department seeks the items of real property and tangible personal property used by WTC during the tax year ending December 31, 2002, and the cost or annual rent of each item. Petitioner objects that this request is "irrelevant and beyond the scope of discovery." The purpose of this interrogatory is to determine any inconsistency in reporting by the Petitioner. Regulation 100.3350(c) states:

Consistency in reporting. In filing returns with this State, if a person departs from or modifies the manner of valuing property, or of excluding or including property in the property factor used in returns for prior years, the person shall disclose in the return for the current year the nature and extent of the modification. If the returns or reports filed by the person with all states to which the person reports under Article IV of the Multistate Tax Compact or the Uniform Division of Income for Tax Purposes Act are not uniform in the valuation of property and in the exclusion or inclusion of property in the property factor, the person shall disclose in its return to this State the nature and extent of the variance.

In 2002, Petitioner included WTC in its Illinois unitary business group and did not exclude WTC pursuant to the 80/20 business activity exemption. Department seeks information showing whether WTC made a substantive change from 2002 to 2007 or merely changed the form of its activities in order to claim an 80/20 business activity exemption in 2007 and 2008. For instance, see the real property figures discussed above concerning Interrogatory 13. Petitioner also objects that the interrogatory is "oppressive and unduly burdensome," "overbroad and vague," and that

the information is not in the Petitioner's control. Petitioner did not otherwise answer the interrogatory. Department asserts that providing schedules G, G-1, G2, E, and H for 2002, as Petitioner did in response to Interrogatories 5, 7 and 13, would be responsive to the Department's request in Interrogatory 14. For these reasons, Department requests this Tribunal overrule Petitioner's objections, and order the Petitioner to provide the information requested.

D. Requests for Production. (To prevent confusion, Department has referred to each discovery request by name, and has not otherwise numbered the following paragraphs.)

Request No. 4. Request No. 4 seeks documentation evidencing Petitioner's answer to Interrogatory 3, which requested "the names,... job titles, job descriptions, and work addresses of the individuals that comprise the [REDACTED] of wages paid by WTC to IBM under the Shared Services Cost Sharing Amendments." Petitioner answers this interrogatory by referencing document number IBM_0001 and, in its Supplemental Response to the Department's First Set of Interrogatories dated October 2, 2015, by referencing and supplying documents numbered IBM_0234 through IBM_0265. These documents provide a job description for certain job titles. However, these documents do not fully answer the Request - specifically, the documents do not evidence the employee's work location(s), or the names and position of their supervisors/managers. The activities of these employees are at the heart of the Business Activity Test. Therefore the Department requests this Tribunal order Petitioner to produce the information requested.

Request No. 5. In Request 5 the Department requests that Petitioner provide access to the U.S. real estate where the directors, officers, and employees of WTC performed their work duties, and the U.S. real property where directors, officers, and employees of IBM performed services on behalf of WTC during the years at issue. Department seeks access to this real estate

in order to determine the value of U.S. real estate used by WTC during the tax years. U.S. real property is one element of the property factor numerator. 100.3350(d). Petitioner objected on the grounds that the request is "unduly burdensome," exceeds the scope of discovery, and is not relevant or will not lead to relevant evidence. Illinois Supreme Court Rule 214 provides:

(a) Any party may by written request direct any other party to produce for inspection, copying, reproduction photographing, testing or sampling specified documents, including electronically stored information as defined under Rule 201(b)(4), objects or tangible things, *or to permit access to real estate* for the purpose of making surface or subsurface inspections or surveys or photographs, or tests or taking samples, or to disclose information calculated to lead to the discovery of the whereabouts of any of these items, whenever the nature, contents, or condition of such documents, objects, tangible things, or real estate is relevant to the subject matter of the action.

Ill. Sup. Ct. Rule 214(a) (Emphasis added). Documents produced by Petitioner (IBM_0025 and 0029, and IBM_0020 and 0027) show WTC paid \$0 of U.S. rent expense and WTC owned \$0 of U.S. real property. Yet, other documents produced by Petitioner show WTC owned [REDACTED] [REDACTED] in New York. IBM_0015. Additionally, Petitioner admits that WTC had 20 employees in New York in 2007 and 2008, respectively. That doesn't add up. If WTC does not own or lease any real property where do its employees work?; where does it keep its machinery and equipment?; and where does it store [REDACTED] dollars of inventory? Department requests the Tribunal overrule Petitioner's objections and order Petitioner to provide the Department's agent with access to the real property at a mutually agreeable time.

Request No. 6 In Request 6., Department requests a copy of Petitioner's organizational chart. In response, Petitioner objected claiming the Department already has a copy. The Department states that the audit file does not contain a copy of Petitioner's organization chart.

Petitioner produced a rudimentary diagram in response to Request No. 6. IBM_0056. However, this organizational chart is deficient because it only outlines the parent, WTC and WTC's subsidiary categories ("Branches," "CFCs," and "LLCs"). An organizational chart, within its plain and ordinary meaning, is a chart that shows the structure of an organization and illustrates relationships between people in the organization. Department requests this Tribunal overrule Petitioner's objections, and order the Petitioner to provide the information requested.

Request No. 7. Taxpayer responded to this request by stating that the officers of WTC did not have employment contracts with WTC. However, this request asks for all "employment contracts for all officers of WTC in effect during the Years at Issue." As such, the Request is not restricted to employment contracts between WTC officers and WTC, rather all such contracts in effect with WTC or any other party, including IBM, are requested. Department requests this Tribunal overrule Petitioner's objections, and order the Petitioner to provide the documentation requested.

Request No. 10. Request 10 asks Petitioner to "Produce Form W-2 for the Tax Years at Issue for all officers of WTC and all domestic individuals that comprise all or part of the [REDACTED] of wages paid by WTC to IBM under the IBM World Trade Corporation Software Intangibles and Shared Services Cost Sharing Amendment, the IBM World Trade Corporation Services Intangibles and Shared Services Cost Sharing Amendment, and the IBM World Trade Corporation Hardware Intangibles and Shared Services Cost Sharing Amendment." In its written response, Petitioner objected asserting the Request was "oppressive and unduly burdensome," "overbroad and vague as to what the Department means by 'wages paid by WTC to IBM,'" and "improper to the extent it seeks an admission of law or requires a legal conclusion, specifically with respect to determining what

constitutes 'wages.'"

The language objected to in Request 10 is taken from the Department's 6/25/15 ICB Action Decision. Petitioner completely understood the phrase "wages paid by WTC to IBM" in the 6/25/14 ICB Action Decision when Petitioner referenced the Action Decision in its Petition. Specifically in paragraphs 58 and 59 of their petition, Petitioner argued the 6/25/14 ICB Action Decision "expressly held that the Department could not impute research and development payroll to WTC from the cost share payment to IBM for purposes of the 80/20 test." Petition, ¶59. The request solicits information regarding the cost share payment by WTC to IBM. This cost share payment comprised wages paid by IBM to its own employees for work specifically allocated through IBM's own accounting principles as research, formation and development of intellectual property and hardware licensed to and sublicensed by WTC. In fact, the amounts listed in the 6/25/14 ICB Action Decision as wages, [REDACTED] [REDACTED] are almost 40 times higher in 2007 and 80 times higher in 2008 than the amount of WTC everywhere payroll as alleged by Petitioner in its own petition - [REDACTED] [REDACTED] (¶27), respectively.

It is wholly within the Department's rights to inquire into the U.S. business activities directly related to the intellectual property that comprises most if not all of WTC's revenues. Whether the amount of wages in the 6/25/14 ICB Action Decision are exact does not abrogate Petitioner's duty to properly respond to this interrogatory. Moreover, the Department has the right to discover facts that may lead to relevant information regarding the "substance over form" of the transactions between IBM and WTC. Department requests this Tribunal overrule Petitioner's objections, and order the Petitioner to provide the documentation requested.

Request No. 11 asks Petitioner to produce documentation of each WTC officer's duties,

including a job description. Petitioner objected and stated that the response was overly broad, vague, oppressive and burdensome and it seeks information outside the Petitioner's possession, knowledge or control. Petitioner stated that WTC does not have documentation of each WTC's officer's duties or job description. If Petitioner does not have the documents, how can providing the documents be oppressive and burdensome? Taxpayer's objection should be overruled. Petitioner's First Supplemental Response to the Department's First Request for Production of Documents identified documents numbered IBM_0195 and IBM_0218 through IBM_0233 as responsive. Not one of these documents provides each officer's duties or a job description. Rather, IBM_0195 simply notes the "Job Title or Role" and IBM_0218 through IBM_0233 simply notes the "Title" of the officer at various entities. Petitioner did not provide the requested information and its objection should be overruled. Accordingly, the Department moves this Tribunal to enter an order compelling Taxpayer to produce the documents requested in Production Request 11.

Request No. 13. In Request 13., Department requests the "travel log for each officer of WTC" and "the travel log for each employee of WTC who traveled to the U.S. on business." In *Zebra*, the court found relevant the fact that individuals other than the sole employee of the Bermuda companies were "in the U.S. performing activities for" the Bermuda companies. Specifically, the court held that quality control activities were performed by the parent in the U.S. The purpose of this request is to determine if WTC officers performed services on behalf of WTC, for instance, by traveling to WTC branches, and to determine if employees of WTC, other than the 20 U.S. employees acknowledged by Petitioner, performed services in the U.S. Petitioner objected on the grounds that the request is "oppressive and unduly burdensome," "irrelevant,"

“overly broad and vague,” and “not in the possession or control of the Petitioner.” If upon a thorough search, Petitioner determines it does not have the requested documents, then Petitioner should confirm the existence of the documents and provide the location of the responsive documents, including the name and address of the custodian, pursuant to Illinois Supreme Court Rule 214, or provide the document retention policy and proof of destruction as requested in Production Request No. 38. Petitioner did not provide the terminology in RTP 13 that is “overly broad and vague.” Petitioner must demonstrate how this request is “oppressive and unduly burdensome.” Ill. Sup. Ct. R. 2301(c)(3). Additionally, the Petitioner is required to maintain its books and records to support any expenses it claimed as a deduction from tax, including travel expenses. 26 U.S. Code § 6001; 86 Ill. Admin. Code § 100.9530(a). For these reasons, the Department requests this Tribunal overrule Petitioner’s objections and order Petitioner to produce the travel logs requested.

Request No. 14. Similarly, in request for production 14., Department requests documentation of travel and entertainment expenses paid by WTC or such expenses incurred by an officer or employee of WTC. Department’s request stated that such documentation included “travel vouchers, travel and entertainment reimbursement requests, travel expense documents, employee expenses reimbursement documents, expense reports, etc.” Petitioner objected that the request is “oppressive and unduly burdensome,” “irrelevant,” “overly broad and vague” because “travel and entertainment” was not defined, and “not in the possession or control of the Petitioner.” Petitioner must show why a request is oppressive and unduly burdensome. Ill. Sup. Ct. R. 201(c)(3). If upon a thorough search, Petitioner determines it does not have the requested documents, then Petitioner should confirm the existence of the documents and provide the location of the responsive documents, including the name and address of the custodian, pursuant

to Illinois Supreme Court Rule 214, or provide the document retention policy and proof of destruction as requested in Production Request No. 38.

"Travel and entertainment" is reported on the U.S. Form 1120, Schedule M-1, Line 5c. The instructions to the U.S. Form 1120 provide an explanation on what may be included in this line and references to the U.S. Code and regulations. Although the Petitioner did not provide a completed copy of Form 1120 for WTC, it must have books and records to substantiate any deduction that flowed to IBM's consolidated return. 26 U.S. Code § 6001; 86 Ill. Admin. Code § 100.9530(a). For these reasons, the Department requests this Tribunal overrule Petitioner's objections and order Petitioner to produce the travel and entertainment documentation requested.

Request No. 15 requests copies of documents ("invoices, bills, statements, contracts, etc.") "evidencing the cost of all training facilities located in the U.S. that were rented by Petitioner and used by an officer or employee of WTC or individuals that comprise all of part of the [REDACTED] wages paid by WTC to IBM through the cost sharing agreements. Petitioner objected and stated that it did not know what was meant by "training facilities." Petitioner also stated that the request was overbroad and improper because it seeks an admission of law or a legal conclusion with respect to "wages." Petitioner also referred to Interrogatory No. 3, which states that Petitioner did not pay the aforementioned sums as wages. The purpose of this request is to determine the cost of facilities (real property) in the U.S. used by an employee or agent of WTC to generate income for WTC through training. Again, documents produced by Petitioner (IBM 0025 and 0029, and IBM 0020 and 0027) show WTC paid \$0 of U.S. rent expense and WTC owned \$0 of U.S. real property. Its officers and employees had to work somewhere, and presumably, required training. Additionally, these

documents could show that agents of WTC conducted training in the U.S. for some foreign WTC employees, which should be allocated to the U.S. payroll factor. Accordingly, Department moves this Tribunal to enter an order compelling Taxpayer to produce the documents requested in Production Request 15.

Request No. 16 seeks a copy of WTC's personnel directory for the Tax Year's at Issue. Petitioner objected by stating that the information was not in Petitioner's control, the request was overly broad and that the Department is already in possession of the requested document, but also stated that it "does not have available a WTC personnel directory for the Tax Years at Issue." The Department's audit file does not contain a copy of WTC's personnel directory. Department is uncertain what documents Petitioner believes the Department has that constitute a personnel directory. A "personnel directory" also known as an "employee directory" or "staff directory," is a compilation of data about employees or contractors of an entity. The data is arranged into fields, which usually include name, title, work division, work location, office/room number, phone number, email address, etc. The data can be maintained either in paper or electronic form. When maintained in electronic form, generally using a database, the data is searchable by field. Petitioner's First Supplemental Response to the Department's First Request for Production of Documents identified documents numbered IBM_0195, IBM_0234, IBM_0266 through IBM_0280 as responsive. None of these documents represent or include a personnel directory. None of the produced documents provides information typically found in a personnel or employee directory, which would likely include: name, work location, work division, phone number, email address, etc. Petitioner did not provide the requested information and its objections should be overruled. Department requests this Tribunal enter an order compelling Taxpayer to produce a personnel directory for WTC employees.

Request No. 18. In request for production 18., the Department seeks documents such as “purchase contracts, leases, subleases, assignments, and agreements,” “evidencing procurement of office, warehouse, facilities or other storage space provided by IBM to WTC and [to] individuals that comprise all or part of the . . . wages paid by WTC to IBM” under the cost sharing agreements. The purpose of this request is to obtain information relevant to the property factor. Petitioner objected that the request is “oppressive and unduly burdensome,” “overly broad and vague” because “wages paid by WTC to IBM” is not defined, “irrelevant,” “not in the possession or control of the Petitioner,” and “duplicative.” However, the language objected to in RTP 18. is taken from the Department’s 6/25/15 ICB Action Decision, which states: “WTC’s payroll factor should not include research & development wages reimbursed to International Business Machines Corporation (“IBM”) by WTC The amounts are [REDACTED] [REDACTED]” Petitioner completely understood the phrase “wages reimbursed to International Business Machines Corporation (“IBM”) by WTC” in the 6/25/14 ICB Action Decision when it referenced the decision in its petition. Specifically in paragraphs 58 and 59 of its petition, Petitioner argued the 6/25/14 ICB Action Decision “expressly held that the Department could not impute research and development payroll to WTC from the cost share payment to IBM for purposes of the 80/20 test.” (Petition, ¶59.) Request No. 18 requests documentation of the value of the real property provided by IBM to WTC and value of real property utilized by the IBM employees for which WTC paid [REDACTED] [REDACTED] to share in the cost of the services they provided. For these reasons, the Department requests this Tribunal overrule Petitioner’s objections and order Petitioner to produce the documentation requested.

Request No. 19. In request for production 19., the Department seeks “documents

evidencing the purchase or rental by IBM of real or tangible personal property located in the united states that was used by WTC in the regular course of business.” The purpose of this request is to obtain information relevant to the numerator of the property factor. Petitioner objected that the request is “oppressive and unduly burdensome,” “not in the possession or control of the Petitioner,” “duplicative,” and “requires a legal conclusion, specifically with respect to determining what constitutes WTC’s “regular course of business.” In response, Petitioner produced summary schedules of beginning and ending balances of tangible personal property by state and “foreign.” First, these documents do not evidence the “purchase or rental by IBM” of property used by WTC. Second, Tribunal has already held that the Department is allowed to look beyond summary information to determine the correctness of the information provided by Petitioner. Order of the Illinois Independent Tax Tribunal, Docket No. 14-TT-229, Order denying Summary Judgment, June 30, 2015 (holding that to require the Department to accept Petitioner’s figures as reported and preclude it as a matter of law from questioning those figures “would turn the law on its head as a Petitioner has the burden of proving clearly it is entitled to” the relief sought.). Finally, as discussed above in Interrogatory No. 13. and Request No. 5., Documents produced by Petitioner (IBM 0025 and 0029, and IBM 0020 and 0027) show WTC paid \$0 of U.S. rent expense and WTC owned \$0 of U.S. real property. Yet, other documents produced by Petitioner show WTC owned [REDACTED] [REDACTED]. (IBM 0015), and that WTC owned [REDACTED] [REDACTED]

IBM 0319. Additionally, Petitioner admits that WTC had 20 employees in New York in 2007 and 2008, respectively. Thus, if the records are correct, another person must be providing WTC with real property (and possibly tangible property) at no charge to conduct its business

operations. For these reasons, the Department requests this Tribunal overrule Petitioner's objections and order Petitioner to produce the documentation requested.

Request No. 20. In request for production 20., Department requests "Schedule G (Beginning and Ending Gross Tangible Property), Schedule G-1 (Beginning and Ending Accumulated Depreciation) and Schedule G2 (Beginning and Ending Net Tangible Property) for WTC for tax years ending December 31, 2002, 2007 and 2008, respectively." Petitioner produced the requested information for tax years ending 2007 and 2008. However, Petitioner objected to the production of documents for the tax year ending December 31, 2002, as irrelevant. The purpose of requesting documentation regarding tax year ending December 31, 2002, is to determine any inconsistency in reporting by the Petitioner. Income Tax Regulation 100.3350(c) states:

Consistency in reporting. In filing returns with this State, if a person departs from or modifies the manner of valuing property, or of excluding or including property in the property factor used in returns for prior years, the person shall disclose in the return for the current year the nature and extent of the modification. If the returns or reports filed by the person with all states to which the person reports under Article IV of the Multistate Tax Compact or the Uniform Division of Income for Tax Purposes Act are not uniform in the valuation of property and in the exclusion or inclusion of property in the property factor, the person shall disclose in its return to this State the nature and extent of the variance.

In 2002, Petitioner included WTC in its Illinois unitary business group and did not exclude WTC pursuant to the 80/20 business activity exemption. Department seeks documentation showing whether WTC made a substantive change from 2002 to 2007 or merely changed the form of its activities in order to claim an 80/20 business activity exemption in 2007 and 2008. Petitioner also objected that the request is "overly broad and vague" and irrelevant." Department requests this Tribunal overrule Petitioner's objections and order Petitioner to provide copies of the

requested schedules for tax years ending December 31, 2002.

Request No. 21 requests documents evidencing real or tangible personal property leased by WTC from January 1, 2002 through December 31, 2002, and the amount of the lease payments. The purpose of requesting documentation regarding tax year ending December 31, 2002, is to determine any inconsistency in reporting by the Petitioner pursuant to Income Tax Regulation 100.3350(c). In 2002, Petitioner included WTC in its Illinois unitary business group and did not exclude WTC pursuant to the 80/20 business activity exemption. Accordingly, the Department moves this Tribunal to enter an order compelling Taxpayer to produce the documents requested in Production Request 21.

Request No. 22. In request for production 22., Department requests documentation of the sale or disposition of each asset shown on WTC's Schedules G, G-1, and G-2 for the tax year ending December 31, 2002 if that asset does not appear on the Schedules G, G1 and G2 for December 31, 2007 or 2008, respectively. The purpose of requesting documentation regarding tax year ending December 31, 2002, is to determine any inconsistency in reporting by the Petitioner pursuant to Income Tax Regulation 100.3350(c). In 2002, Petitioner included WTC in its Illinois unitary business group and did not exclude WTC pursuant to the 80/20 business activity exemption. Department seeks documentation showing whether WTC made a substantive change from 2002 to 2007 or merely changed the form of its activities in order to claim an 80/20 business activity exemption in 2007 and 2008.

Request No. 23 requested WTC's balance sheet and income statement for the tax years ending December 31, 2006, 2007 and 2008. Petitioner produced a copy of the 2006, 2007 and 2008 Schedule L (Balance Sheet per Books), from its US Corporation Income Tax Returns (US 1120) but did not tender a copy of the detail statements for Schedule L for each of the tax years.

Additionally, Petitioner did not tender a copy of WTC's income statement for the aforementioned tax years. The Department seeks a copy of the detail statements to the Schedule L, a copy of WTC's GAAP (Generally Accepted Accounting Principles) balance sheet and income statement for each of the aforementioned tax years. Accordingly, the Department moves this Tribunal to enter an order compelling Taxpayer to produce the documents requested in Production Request 23.

Request No. 24. Request 24 seeks copies of reports documenting internal audits of WTC conducted by WTC, IBM, or a third party. The term "internal audit" is commonly used in the industry. The request is even broader as it asks for not only internal audits conducted by IBM, WTC or third parties but any evaluations or analysis of the operations or activities of WTC. The issue in this matter is whether WTC meets the 80/20 exemption based on the business activity of WTC in the U.S. and abroad. Internal audit reports, findings, memos, emails, etc. would all be relevant documents for the Department to review in preparing its case as they may provide a discussion or analysis of WTC's activities, certain property or payroll. To the extent any documents responsive to this request are privileged, Taxpayer must produce a privilege log to the Department that identifies the documents withheld and the privilege asserted. A blanket privilege objection does not suffice. Illinois case law provides that the party claiming the privilege has the burden of showing the facts that give rise to the privilege. *Mlynarski v. Rush Presbyterian-St. Luke's Medical Center*, 213 Ill. App. 3d 427, 431 (1991). Privileges are strongly disfavored and must be strictly construed as an exception to the general duty to disclose. *In re Marriage of Daniels*, 240 Ill. App.3d 314, 324-25, 607 N.E.2d 1255 (1992). Department requests this Tribunal order Petitioner to produce the documents in Request No. 24.

Request No. 26. Request 26 requests WTC's Board of Directors' minutes, committee

minutes, agendas, resolutions, and consents. With regard to Taxpayer's claim of privilege regarding the WTC Directors meetings, committee minutes, agendas resolutions, please see the argument regarding Request No. 24 above. In its supplement, Petitioner provided various consents in lieu of meetings, however, it is unclear whether there were no other meetings of the Directors, or committee meetings, agendas or other resolutions. The Department needs all responsive documents before conducting depositions. Department requests the Tribunal order Petitioner to provide any additional responsive documents, or a written response stating there are no other responsive documents.

Request No. 27. Request 27 asks Petitioner to produce IBM's Board of Directors' meeting minutes, committee minutes, agendas, resolutions, and consents. These documents may contain relevant information regarding WTC's activities, activities conducted by IBM for the benefit of WTC, the cost-sharing agreements, and cost sharing payments. These documents are not in the possession of the Department. To the extent any documents responsive to this request are privileged, Taxpayer must produce a privilege log to the Department that identifies the documents withheld and the privilege asserted, pursuant to Illinois Supreme Court Rule 201(n). Department requests the Tribunal overrule Petitioner's objections and order Petitioner to provide all responsive documents.

Request No. 28. In request for production 28., Department requests "documentation evidencing the square footage of any facility located in the United States (including U.S. territories) that was owned or leased by IBM and used by an officer, director, or employee of WTC during the years at issue." The purpose of the request is to aid in determining the value of the real property used by WTC for which no rent was paid. 86 Ill. Admin. § Code

100.3380(b)(2). ("If property owned by others is used by the person at no charge or rented by the person for a nominal rate, the net annual rental rate for the property shall be determined on the basis of a reasonable market rental rate for such property."). Petitioner objected that the request is "oppressive and unduly burdensome," "irrelevant," "not in the possession or control of the Petitioner," "duplicative," and "overly broad and vague." In its supplemental response of October 2, 2015, Petitioner produced IBM [REDACTED] which described the amount of square feet of office space for different employee categories. However, this information does not provide "the square footage of any facility located in the United States (including U.S. territories) that was owned or leased by IBM and used by an officer, director, or employee of WTC during the years at issue." The documents provided do not identify the facility or the total amount of square feet used by WTC. Department requests this Tribunal overrule each objection and order the Petitioner to provide the documentation requested.

Request No. 30 asks Petitioner to produce a copy of "all employment manuals, policy and procedure guides, handbooks, and/or corporate information applicable to WTC employees" during the Tax Years at Issue. Petitioner objected to the Department's request stating it was irrelevant, not reasonably calculated to lead to the discovery of admissible evidence and the information is not in Petitioner's possession or control. Manuals showing common policies, procedures or direction for services or guidance are relevant to determine if IBM performs services on behalf of WTC. This documentation is relevant to both the payroll and property factors in determining whether WTC's business activity outside the United States is 80% or more of its total activity. Petitioner, in its First Supplemental Response to the Department's First Request for Production of Documents, now states that WTC does not have employment manuals, policy and procedure guides or handbooks during the Tax Years at Issue. The Department asked

for "employment manuals, policy and procedure guidelines, handbooks, and/or corporate information *applicable to* WTC employees." If WTC did not have its own policy manuals, then almost certainly the policy manuals of IBM covered WTC employees. These documents are responsive to the Department's request. If the documentation is truly not in Petitioner's possession, Petitioner must identify the documents and the custodian as required by Illinois Supreme Court Rule 214, or provide the document retention policy and proof of destruction as requested in Production Request No. 38. Accordingly, the Department moves this Tribunal to enter an order compelling Taxpayer to produce the documents requested in Production Request 30.

Request No. 31 asks Petitioner to produce *all* agreements between WTC and IBM. Petitioner produced some agreements. Pursuant to Definition 27., "IBM' means International Business Machines Corporation [REDACTED] including its *subsidiaries*, affiliates, agents and assigns." Department requests a copy of the sub-licensing agreements between WTC and any subsidiary or affiliate of IBM that were in effect during the Tax Years at Issue. This agreement should reveal the duties of the parties, and therefore, is relevant to the payroll factor in determining whether WTC's business activity outside the United States is 80% or more of its total activity. Department requests this Tribunal enter an order compelling Taxpayer to produce the documents requested in Production Request 31.

Request No. 32. In request for production 32., Department requests the transfer pricing studies Petitioner referenced in its Petition. Petition, ¶¶ 20, 21. Petitioner objected that this request is "oppressive and unduly burdensome," "overly broad and vague," and "irrelevant." Petitioner also asserted "attorney-client privilege, accountant-client privilege, attorney work-

product doctrine, or another privilege.” First, Illinois law does not provide a privilege to a client for accountant-client communications. *Brunton v. Kruger*, 2015 IL 117663, ¶¶33-46. (“We hold that the privilege created by section 27 of the Public Accounting Act is held by the accountant and may be asserted or waived by him.”). As IBM is not an accountant, but rather the client, it cannot assert an accountant privilege. Regarding the attorney-client privilege and work product doctrine, Illinois Supreme Court Rule 201 provides:

(b) *** (2) Privilege and Work Product. All matters that are privileged against disclosure on the trial, including privileged communications between a party or his agent and the attorney for the party, are privileged against disclosure through any discovery procedure. Material prepared by or for a party in preparation for trial is subject to discovery only if it does not contain or disclose the theories, mental impressions, or litigation plans of the party's attorney. The court may apportion the cost involved in originally securing the discoverable material, including when appropriate a reasonable attorney's fee, in such manner as is just.

(n) Claims of Privilege. When information or documents are withheld from disclosure or discovery on a claim that they are privileged pursuant to a common law or statutory privilege, any such claim shall be made expressly and shall be supported by a description of the nature of the documents, communications or things not produced or disclosed and the exact privilege which is being claimed.

Ill. Sup. Ct. Rule 201(b)(2), (n). Here, Petitioner has not provided a privilege log as required by Rule 201(n). Additionally, Petitioner has waived any privilege it could assert to the transfer pricing studies. In *Center Partners, Ltd. v. Growth Head GP, LLC*, 2012 IL 113107, the Illinois Supreme Court examined the issue of waiver of the attorney-client privilege. The Court held:

Among the exceptions to the attorney-client privilege is the concept of “waiver.” The attorney-client privilege belongs to the client, rather than the attorney, although the attorney asserts the privilege on behalf of the client. Only the client may waive the privilege. The attorney, although presumed to have authority to waive the privilege on the client's behalf, may not do so over the client's objection. “Any disclosure by the client is inherently inconsistent with the policy behind the privilege of facilitating a

confidential attorney-client relationship and, therefore, must result in a waiver of the privilege.” Thus, for example, the attorney-client privilege may be waived by the client when the client voluntarily testifies to the privileged matter, or when the client voluntarily injects into the case either a factual or legal issue, the truthful resolution of which requires examination of confidential communications, such as legal malpractice actions. The basic, well-settled rule is that when a client discloses to a third-party a privileged communication, that particular communication is no longer privileged and is discoverable or admissible in litigation.

¶ 39 The purpose behind the doctrine of subject matter waiver is to prevent partial or selective disclosure of favorable material while sequestering the unfavorable. “This is so because the privilege of secret consultation is intended only as an incidental means of defense, and not as an independent means of attack, and to use it in the latter character is to abandon it in the former.” Courts have characterized this reasoning as the “sword” and the “shield” approach, in that a litigant should not be able to disclose portions of privileged communications with his attorney to gain a tactical advantage in litigation (the sword), and then claim the privilege when the opposing party attempts to discover the undisclosed portion of the communication or communications relating to the same subject matter.

Center Partners, Ltd. v. Growth Head GP, LLC, 2012 IL 113107, ¶¶ 35-39.

Petitioner made factual allegations in its Petition upon which it relies to support WTC's 80/20 business activity exemption from Illinois tax. Petition, ¶¶20-21. Specifically, Petitioner alleged that:

20. IBM and WTC have periodically amended these agreements to adjust the hardware royalty rates and software royalty rates according to updated transfer pricing studies.
21. The most recent software royalty transfer pricing study indicated that the royalty is within the interquartile range for comparable uncontrolled software license transactions.

Petition, ¶¶20-21. Because the Petitioner is using the claimed privilege information as a sword – to support its calculation of royalty payments from WTC to IBM - any privilege asserted should be deemed waived by Petitioner, and Department should be allowed to investigate what additional

information was contained in the transfer pricing studies that may not support the Petitioner's argument. *Center Partners, Ltd. v. Growth Head GP, LLC*, 2012 IL 113107, ¶39. Department requests this Tribunal overrule the Petitioner's objections, hold that the accountant privilege does not apply to Petitioner, find that any privilege to the transfer pricing studies was waived, and order the Petitioner to produce the transfer pricing studies.

Request No. 33 requests all bank statements for accounts maintained by WTC both inside and outside of the United States for the Tax Years at Issue. Petitioner objected and stated that the request was overly broad, vague, and irrelevant, would not lead to the discovery of admissible evidence and that the Department already possesses said documents. This request is relevant to both the payroll and property factors – paying employees and purchasing tangible personal and real property – in determining whether WTC's business activity outside the United States is 80% or more of its total activity. The Department states that its audit file does not contain a copy of WTC's bank statements. In the alternative, the Department requests WTC's bank information including the name of the bank(s), address(es), and account number(s). Department requests this Tribunal enter an order compelling Taxpayer to produce the documents requested in Production Request 33.

Request No. 34 seeks various documents pertaining to the location of real property that was used by an officer, director employee or agent of WTC in the United States or its territories during the Tax Years at Issue. Petitioner objected claiming the request was oppressive and unduly burdensome, irrelevant and beyond the scope of discovery and states that the information is not within its possession, knowledge or control. Petitioner also stated that the request is improper because it seeks an admission of law or a legal conclusion. Petitioner also responded that the Department already has possession of said documents. This request for the location of

real property used by WTC is relevant to the property factor in determining whether WTC's business activity outside the United States is 80% or more of its total activity. The Department states that its audit file does not contain a copy of documents pertaining to real property used by Petitioner.

Petitioner, in its First Supplemental Response to the Department's First Request for Production of Documents, produced documents that are unresponsive to the Request. Petitioner produced documents numbered IBM_0195 and IBM_0234, which includes the identity of the WTC Officers, Officer W-2s and identity of WTC Employees, which are not documents pertaining to owned or leased real property that was used by WTC in the United States or its territories. Accordingly, the Department moves this Tribunal to enter an order compelling Taxpayer to produce the documents requested in Production Request 34.

Request No. 35 seeks documents pertaining to Interrogatory Number 6, (which requests the location of real property where an officer, director, employee or agent of Petitioner/IBM performed services on behalf of WTC), "including but not limited to all approval committee meeting notes and minutes, all notes, memorandums, emails, correspondence between officers, directors, employees of IBM and WTC regarding all federals, state and local permits and licenses, mortgages, leases, contracts for deed, subleases, assignments, sales agreements, liens or other encumbrances, construction agreements, addendums, riders, all documents evidencing ownership including deeds, certificates of transfer, title commitments, UCC filings, Section 1031 transfers, escrow account statements or any other like documents."

Petitioner objected to Request 35 claiming the request was oppressive and unduly burdensome, overly broad and vague as to what "performed services ... on behalf of WTC" means, irrelevant and not reasonably calculated to lead to the discovery of admissible evidence,

duplicative or cumulative, beyond the scope of discovery and not within its possession, knowledge or control, and improper because it seeks an admission of law or a legal conclusion in determining who was an "agent" of IBM and what "on behalf of WTC" means. Petitioner also stated that the Department already has possession of said documents.

Again, the Department is seeking documents regarding the real property used by WTC during the Years at Issue. This request is relevant to the property factor in determining whether WTC's business activity outside the United States is 80% or more of its total activity. The Department states that its audit file does not contain the information requested. Accordingly, the Department moves this Tribunal to enter an order compelling Taxpayer to produce the documents requested in Production Request 35.

Request No. 36 seeks documents evidencing Petitioner's response to Interrogatory No. 7, which concerns the cost, lease amount or fair market value for all tangible personal property used by an officer, employee, or agent of WTC in performing services on behalf of WTC within the United States and its territories. The Department produced a non-exhaustive list of tangible personal property. Petitioner objected to Request 36 claiming the request was oppressive and unduly burdensome, overly broad and vague as to what "performed services ... on behalf of WTC" means, irrelevant and not reasonably calculated to lead to the discovery of admissible evidence, and improper because it seeks an admission of law or a legal conclusion. Petitioner also stated that the Department already has possession of said documents.

Petitioner, in its First Supplemental Response to the Department's First Request for Production of Documents produced a variety of charts that are labeled "BEG Gross Tangible Property Year 2007," "BEG ACC Depreciation Year 2007," "BEG Net Tangible Property Year 2007," "END Gross Tangible Property Year 2007," "END ACC Depreciation Year 2007,"

“END Net Tangible property Year 2007,” “Rent Expenses Year 2007,” “AVG Gross Tangible Property Year 2007,” “AVG Net Tangible Property Year 2007,” “Payroll with Partnerships Year 2007,” “Payroll without Partnerships Year 2007,” and the same documents for tax year 2008. While Petitioner produced a variety of documents, the documents are not responsive because they do not disclose the cost, lease amount, or fair market value for all of the tangible personal property used by an officer, employee, or agent of WTC in performing services on behalf of WTC within the United States and its territories. This information is relevant to calculating the property factor. Therefore, the Department moves this Tribunal to enter an order compelling Taxpayer to produce the documents requested in Production Request 36.

Request No. 37 seeks documents pertaining to Interrogatory No. 8, which concerns the cost, lease amount or fair market value for all tangible personal property used by an officer, employee, or agent of IBM in performing services on behalf of WTC within the United States and its territories. The Department produced a non-exhaustive list of tangible personal property. Petitioner objected and claimed this request was oppressive and unduly burdensome and stated it did not have any knowledge, control or possession of the information. Petitioner claimed the term “performed services” on behalf of WTC is vague.

Request 37 is relevant to the property factor in determining whether WTC's business activity outside the United States is 80% or more of its total activity. In the alternative, the Department requests a copy of IBM's inventory sheet/document, purchase orders and a depreciation schedule for tangible personal property used by IBM officers, employees, or agent in performing services on behalf of WTC within the United States and its territories during the Tax Years at Issue. Accordingly, the Department requests this Tribunal enter an order compelling Taxpayer to produce the documents requested in Production Request 37.

Request No. 38. Request 38 requests the document retention policy for each document that Petitioner was unable to locate or that was destroyed. Every publically traded company maintains a written record retention policy to ensure compliance with IRS and SEC rules. (*See for example* 26 U.S. Code § 6001, 274(d), 280F(d)(4); 17 CFR Part 210.) Petitioner has claimed that certain documents are not in its possession or control. If responsive documents were destroyed, the Department has a right to know whether Petitioner followed the written record retention policy in effect.

E. Conclusion

34. The purpose of discovery is the ascertainment of truth and to promote either a fair settlement or a fair trial. *Computer Teaching Corp. v. Courseware Applications, Inc.*, 199 Ill. App. 3d 154, 157 (4th Dist. 1990).

35. Another purpose is to eliminate surprises so that a judgment will rest upon the merits, and not upon the skillful maneuvering of counsel. *Mistler v. Mancini*, 111 Ill. App. 3d 228, 232 (2d Dist. 1982).

WHEREFORE, for the foregoing reasons, the Department moves this Tribunal to enter an order compelling Petitioner to respond in full to the Department's First Set of Interrogatories and First Request for Production of Documents.

Respectfully submitted,

LISA MADIGAN
ATTORNEY GENERAL, STATE OF ILLINOIS

By:



Special Assistant Attorney General

Susan Budzileni
(312) 814-1716
Susan.Budzileni@Illinois.gov

Department's Motion to Compel
Docket No. 14-TT-229

Sean Cullinan
(312) 814- 3078
Sean.Cullinan@illinois.gov

Jennifer Kieffer
(312) 814-1533
Jennifer.Kieffer@Illinois.gov

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

Facsimile: (312) 814-4344

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