

**IT 10-05**

**Tax Type: Income Tax**

**Issue: Net Operating Loss Carryback**

**STATE OF ILLINOIS  
DEPARTMENT OF REVENUE  
OFFICE OF ADMINISTRATIVE HEARINGS  
CHICAGO, ILLINOIS**

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CHICAGO, ILLINOIS**

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<b>THE DEPARTMENT OF REVENUE OF THE STATE OF ILLINOIS</b>	)	<b>No.:</b>	<b>09-IT-0000</b>
	)	<b>Account ID:</b>	<b>00000-00000</b>
	)		
<b>v.</b>	)		
	)		
<b>ABC MACHINING, INC.,</b>	)	<b>Julie-April Montgomery</b>	
<b>Taxpayer.</b>	)	<b>Administrative Law Judge</b>	

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**ORDER PURSUANT TO THE DEPARTMENT'S MOTION FOR SUMMARY  
JUDGMENT**

This cause arose from a protest filed by ABCs Machining, Inc. ("Taxpayer") of the Notice of Deficiency ("NOD") dated August 17, 2009 and issued by the Illinois Department of Revenue ("Department"). The NOD was issued pursuant to the provisions of the Illinois Income Tax Act ("IITA"), 5 ILCS 5/101 *et seq.* The Department adjusted Taxpayer's Net Loss Deduction ("NLD") to agree with its records.

The Department filed a "Motion for Summary Judgment" ("Mn."). In response, Taxpayer filed "Taxpayer, ABC Machining, Inc., Response Brief to Department's Motion for Summary Judgment" ("TR"), and the Department subsequently filed "Department's Reply to Taxpayer's Response Brief to the Department's Motion for Summary Judgment" ("DR").

The issue presented is whether Taxpayer was required to check the box on its 2001 and 2002 Illinois IL-1120 Returns (“Return”) so that it could forgo the Illinois NLD carryback periods. Following a review of the briefs filed by the parties, Summary Judgment is granted in favor of the Department. In support of this determination are made the following findings of fact and conclusions of law.

**Findings of Fact:**

1. On August 17, 2009, the Department issued to Taxpayer a NOD that determined Taxpayer owed tax and interest for the November 2007 reporting period. This NOD was attached to the Department’s Motion under a certificate of the Director of Revenue entitled “Certification of Records.” Mn. Ex. No. 7 (“Notice of Deficiency for Net Loss Deduction”).
2. The Department adjusted Taxpayer’s NLD to agree with Department records and as a consequence recomputed Taxpayer’s liability for the November 2007 reporting period. *Id.* (“Statement: Reasons for Deficiency”).
3. Taxpayer filed a “Schedule NLD: Illinois Net Loss Deduction” for the year ending November 2007 wherein Taxpayer carried forward its Illinois net loss of \$85,080 for the loss year that ended November 2001 to tax reporting periods that ended on November 2004 and November 2005. Mn. Ex. No. 1 (2006 Form IL-1120).
4. Taxpayer reported an Illinois net loss of \$136,346 for the loss year that ended November 2002. *Id.*
5. Taxpayer reported an Illinois net loss of \$13,684 for the loss year that ended November 2003. *Id.*
6. Taxpayer did not check the box on its Return for the reporting period that ended November 2001 (“2001 period”) that requested Taxpayer “Check [the] box if [Taxpayer was] electing to forgo the Illinois NLD carryback period.” Mn. Ex.

- No. 2 (November 2001 Return).
7. Taxpayer did not carry back its 2001 NLD to 1999, a year in which it had income against which this NLD could have been offset. Taxpayer did not have income against which a NLD could have been offset in 2000. Mn. Ex. No. 1.
  8. Taxpayer also failed to check the box to elect to forgo the NDL carryback period on its Return for the reporting period that ended November 2002 (“2002 period”). Mn. Ex. No. 3 (November 2002 Return).
  9. Taxpayer did not carry back its 2002 NLD because it had no losses for the years 2000 and 2001 upon which this NLD could have been offset. Mn. Ex. No. 1; Mn. p. 8
  10. Taxpayer did check the box on its Return for the reporting period that ended November 2003 (“2003 period”) electing to forgo the Illinois NLD carryback period. Mn. Ex. No. 4 (November 2003 Return).
  11. Taxpayer’s protest, in this matter, states that its “[a]ccountant did not check a box for loss carried forward.” Mn. Ex. No. 8 (Taxpayer’s income tax protest).
  12. The Department determined Taxpayer could not carry forward its reported \$84,952 Illinois net loss from the 2001 period to the reporting periods that ended November 2004 and November 2005. Mn. Ex. Nos. 2; 5 (Department’s correction of the November 2007 Schedule NLD).

### **Conclusions of Law**

A motion for summary judgment is appropriate where no genuine issue of material fact exists such that the moving party is entitled to judgment as a matter of law. Busch v. Graphic Corp., 169 Ill. 2d 325 (1996). Summary judgment is a drastic means of disposing of litigation and therefore is permitted only when the right of the moving party is clear and free from doubt. Purtill v. Hess, 111 Ill. 2d 229, (1986). To determine

whether a genuine issue of material fact exists, one must consider the pleadings, depositions, admissions, exhibits and affidavits on file which must be strictly construed against the movant and in favor of the non-movant. *Id.* The burden is upon the movant to demonstrate there are no genuine issues of material fact. Guese v. Farmers Inter-Insurance Exchange, 238 Ill. App. 3d 196, 200 (1<sup>st</sup> Dist. 1992). “A triable issue precluding summary judgment exists where the material facts are disputed or where, the material facts being undisputed, reasonable persons might draw different inferences from the undisputed facts.” Williams v. Manchester, 228 Ill. 2d 404, 417 (208). If the movant furnishes facts which, if not contradicted, would entitle movant to judgment as a matter of law, the opposing party cannot rely on its pleadings alone to raise issues of material fact. Purtill at 240-241. Thus, facts contained in documentation in support of a motion for summary judgment which are not contradicted by affidavit are admitted and must be taken as true for the purposes of the motion for summary judgment. *Id.* at 241.

The IITA, during the years 2001 and 2002, provided:

(a) If applying all of the modifications provided for in paragraph (2) of Section 203(b), paragraph (2) of Section 203 (c) and paragraph (2) of Section 203(d) and the allocation and apportionment provisions of Article 3 of this Act, the taxpayer’s net income results in a loss...

(2) for any taxable year ending on or after December 31, 1999, such loss shall be allowed as a carryback to each of the 2 taxable years preceding the taxable year of such loss and shall be a net operating carryover to each of the 20 taxable years following the taxable year of such loss.

(A) The taxpayer may elect to relinquish the entire carryback period with respect to such loss. Such election shall be made in the form and manner prescribed by

the Department and shall be made by the due date (including extensions of time) for filing the taxpayer's return for the taxable year in which such loss is incurred, and such election, once made, shall be irrevocable.

(B) The entire amount of such loss shall be carried to the earliest taxable year to which such loss may be carried. The amount of such loss which shall be carried to each of the other taxable years shall be the excess, if any, of the amount of such loss over the sum of the deductions for carryback or carryover of such loss allowable for each of the prior taxable years to which such loss may be carried. 35 ILCS 5/207(a).

To summarize, section 207(a) of the IITA mandates a NLD be carried back to the earlier of the two preceding years of the NLD in which Taxpayer had net income before the NLD can be applied to years that are subsequent to the year in which the NLD arose. Hence, if it is determined that Taxpayer failed to make an election to forgo its two year NLD carryback period ("Election") as required by section 207(a) of the IITA, the Department's motion for summary judgment must be granted.

The Department argues that Taxpayer's failure to check the box forgoing carrybacks of losses for the 2001 period and 2002 period established Taxpayer carry back the NLDs for these periods before it could carry these NLDs forward. The Department further argues that the absence of the Election required the NLDs be carried back before they could be carried forward. Mn. pp. 6-7.

Taxpayer posits four arguments in response to the Department's position. First, the instructions with respect to the "IL-1120 return form [were] not law and should not rule this case." TR p. 6. Second, Taxpayer made "a de facto [or implicit] election to

forgo any carryback.” *Id.* at 3. Third, Taxpayer was taxed twice. *Id.* at 6. Fourth, the Department failed to make a timely determination of the tax due. *Id.* at 5.

Section 207(a)(2) stated a “loss shall be allowed as a carryback to each of the 2 taxable years preceding the taxable year of such loss and shall be a net operating carryover to each of the 20 taxable years following the taxable year of such loss.” 35 ILCS 5/207(a)(2). The exception to this mandated procedure which allowed the relinquishment of the entire carryback period (i.e. 2 years) in favor of only being able to carry the loss (or NLD) forward was stated in section 207(a)(2)(A). Section 207(a)(2)(A) permitted the forfeiture of the entire carryback period if “made in the form and manner prescribed by the Department”. 35 ILCS 5/207(a)(2)(A). This provision also stated that once such Election was made it was “irrevocable.” *Id.* In addition, section 207(a)(2)(A) specifically stated that the Election “shall be made by the due date (including extensions of time) for filing the taxpayer’s return.” *Id.*

In summary, section 207(a)(2)(A) stated that if Taxpayer did not make the Election, the NLD was first carried back. In addition, only after the NLD had been carried back to offset income for each of the two years before the year of the loss, could any remaining portion of the NLD be carried forward. Conversely, if the Election was made, Taxpayer could have carried forward its loss for up to 20 years succeeding the year of the loss without carrying any portion of the NLD back. However, the ability to only carry forward the NLD required the Election be made, as required by Illinois law.

Pursuant to 35 ILCS 5/1401(a) the “Department is authorized to...prescribe such forms, relating to the administration and enforcement of the provisions of [the IITA], as it may deem appropriate.” 35 ILCS 5/1401(a). In addition, 35 ILCS 5/1501(a)(19) states

the “term ‘regulations’ includes ...forms prescribed by the Department.” 35 ILCS 5/1501(a)(19).

The manner and form in which the Election debuted was in the 1996 Return instructions. These instructions stated “What’s New for 1996...A new box has been added to the form for the purpose of electing to forgo the Illinois net loss deduction carryback period”. 1996 IL-1120 Instructions. For the 2001 period and 2002 period these instructions provided:

Illinois net losses must be carried back 2 years (unless an election to only carry the losses forward is made), then forward 20 years.

**Note:** You may make the election to only carry the loss forward and to forgo the Illinois NLD carryback period by checking the box below Part IV, Line 1. This election must be made by the extended due date of the loss year return.

**Once made, the election is irrevocable.** (Emphasis in the original). *Id.*

These instructions made clear that the only procedure for the Election was to check the box contained below Part IV, Line 1 of the Return. This was the affirmative act required of Taxpayer if it wished to both express its intent and exercise its option to forgo its NLD carrybacks.

Taxpayer does not dispute that it failed to check the box provided below Part IV, Line 1 of its Returns. In fact, Taxpayer admits that the box addressing the Election on its Returns was an “administrative error” attributable to its “Accountant.” Mn. Ex. No. 8; TR p. 6. In light of this admission and failure to check the boxes on Taxpayer’s Returns, it is clear Taxpayer did not make the Election as prescribed by Illinois law.

Taxpayer argues “an implicit election could occur in the absence of language in the Illinois regulation Section 100.2330 requiring the taxpayer check a box on the tax

return. The requirement to check a box in order to forgo carryback is not in the language of the Illinois code or regulations, therefore an implicit election could be made.” TR p. 5. This argument is without merit.

As previously noted, a specific method for exercise of the Election was established in 1996. In accordance with both the amended Regulation and the IITA, the Return was amended to provide a specific box to be checked if there was to be an Election. Hence, Taxpayer’s argument that there was an absence of language on how to make the Election is both meritless and contrary to the law.

Taxpayer also alleges that the Regulation substantiates its position that “carrying the loss forward is an implicit election to forgo any carryback.” TR p. 4. Taxpayer’s argument is misplaced and ignores the 1996 amendment. The amended Regulation, applicable to this case, specifically requires the election “shall be made on the taxpayer’s return for the taxable year in which the loss is incurred.” 86 Ill. Admin. Code Section 100.2330(b)(1). This Regulation made no mention that the option to forgo the carryback period could have been implied because Taxpayer carried its loss forward. Furthermore, Taxpayer has cited no authority, and none has been found, to support the argument that an “implicit” Election could have been made. The amended Regulation affords Taxpayer no support for its “implicit” Election argument.

Taxpayer cites Department letter ruling IT-97-0098-GIL<sup>1</sup> (“GIL”) in support of its assertion that “an implicit election [could have been] allowed by simply carrying the loss forward.” TR. p. 4. This GIL however refutes Taxpayer’s assertion. This GIL states:

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<sup>1</sup> While Taxpayer refers to this letter as a Private Letter Ruling (“PLR”), the letter itself clearly states the Department was “respond[ing] with a GIL. IT-97-0098-GIL. The distinction being a PLR is binding upon the Department but only as to the taxpayer who is the subject of the request in contrast to a GIL (or General Information Letter) which “does not constitute statements of agency policy that apply, interpret or prescribe the tax law and [is] not binding on the Department.” *Id.*

Effective September 27, 1996, the Department promulgated a regulation (i.e. 86 Ill. Adm. Code Section 100.2330, copy enclosed) under which a taxpayer may elect to forego the carryback period by checking the appropriate box on the tax return for the year in which the taxpayer incurred the...NLD. Prior to the effective date of this regulation, a taxpayer could make the election to forego the carryback period...by filing a return carrying the loss forward before filing a return carrying the loss back. IT-97-0098-GIL.

In light of the Department's statement in the GIL, it is clear that losses incurred after 1996 required Taxpayer to check the appropriate box on the Return for the years in which Taxpayer incurred losses.

Taxpayer incurred its losses in 2001 and 2002. Returns filed by Taxpayer contained unchecked boxes thereby evidencing the Election had not been made. The GIL supports a conclusion that when one fails to check the appropriate box for periods subsequent to 1996, as Taxpayer did here, there can be no Election.

Taxpayer rightly states the Department found "taxpayer could implicitly make the election to forego the carryback period by filing a return carrying the loss forward before filing a return carrying the loss back" (IT-97-0098-GIL; TR p. 4) for a loss incurred in 1995. The 1995 loss was prior to the Department's 1996 amendment of the Regulation. Thus, Taxpayer's reliance on the GIL is an argument without merit.

On its 2003 Return, Taxpayer checked the Election box to forgo the two year carryback period. Such action illustrates that Taxpayer was aware that a check of the Election box was the required procedure to forgo the two year carryback period.

Taxpayer states that it has been "taxed twice; once in the year at issue, 2007, and again for the income in the closed year, 1999, since it is precluded from obtaining the benefit of a carryback." TR p. 6. Taxpayer, by its failure to follow Illinois law by not

checking the Election box on its 2001 Return, and because of Taxpayer's inaction to timely file for a refund for the 1999 year, placed itself in the situation of which it now complains. It was Taxpayer that subjected itself to being "twice taxed" on its income, not the Department. The Department was unaware of Taxpayer's situation until 2008 when the Return for the period ending November 2007 was filed. Upon the filing of the 2007 Return, the Department discovered Taxpayer's failure to check the box for the Election on its 2001 Return and, as such, the Department had no choice but to apply Illinois Law and carry back the 2001 NLD to 1999. Inasmuch as Taxpayer failed to file a request for a refund in a timely fashion, no refund can be awarded Taxpayer. There was no law cited by Taxpayer, nor has any law been found, that states the taxation of Taxpayer twice as occurred here is prohibited. Hence, this argument fails to support Taxpayer's position that it should have been able to utilize its 2001 NLD in years subsequent to 2001 as opposed to years prior to 2001.

Taxpayer contends section 904(a) of the IITA placed upon the Department "a duty to access both under and over payments by a taxpayer's filed return. And do so as soon as practicable after a return is filed." TR p. 5. Taxpayer states that the "2004 return clearly show[ed] a carryforward from 2001. The Department did not examine the 2004 return in a timely, practicable manner...and [so] unfairly disadvantaged the Taxpayer by inconsistently applying Section 904(a)." *Id.* at 5-6. This argument is baseless.

The Return at issue is for the year ending November 2007, not the years that end on November 2001 or November 2004. Taxpayer completed its Return for the period ending November 2007 on May 28, 2008. Mn. Ex. No. 1. The Department issued the NOD on August 17, 2009. The Department notified Taxpayer of its disagreement with

Taxpayer's Return for the tax year ending November 2007 well before the running of the three year statute of limitations for the issuance of the NOD. 35 ILCS 5/905(a). Thus, there is nothing to suggest that the Department failed to act according to statutory mandates.

Section 904(a) of the IITA provides that the admission into evidence of the NOD establishes the Department's *prima facie* case and is *prima facie* evidence of the correctness of the amount due. 35 ILCS 5/904(a); PPG Industries, Inc. v. Department of Revenue, 328 Ill. App. 3d 16, 33 (1<sup>st</sup> Dist. 2002); Balla v. Department of Revenue, 96 Ill. App. 3d 293, 296-97 (1<sup>st</sup> Dist. 1981). The burden is then on the taxpayer to rebut the correctness of the notice. *Id.* Once the Department's *prima facie* case is established, the burden of proof is shifted to the taxpayer to overcome the Department's *prima facie* case. Clark Oil & Refining Corp. v. Johnson, 154 Ill. App. 3d 773 (1<sup>st</sup> Dist. 1987).

In order to overcome the presumption of validity attached to the Department's *prima facie* case, taxpayer must produce competent evidence, identified with its books and records that show the Department's determination is incorrect. A.R. Barnes & Co. v. Department of Revenue, 173 Ill. App. 3d 826 (1<sup>st</sup> Dist. 1988).

The Department's NOD was attached to its motion, under the certificate of the Director of Revenue, and as such, the Department's *prima facie* case was established, and the burden of proof shifted to Taxpayer to overcome the Department's *prima facie* case.

Taxpayer only posited one document. This document restated the same numbers Taxpayer listed on its Schedule NLD for the carry year ending November 2007 (and it was these same numbers that were subsequently corrected by the Department and resulted in the NOD at issue). This document presents no genuine issue of material fact.

This document and Taxpayer's arguments do not contradict the fact that Taxpayer admittedly failed to check the Election box on its 2001 and 2002 Returns.

Taxpayer seeks to carry forward, not back, its 2001 and 2002 NLDs. However, as previously stated, Taxpayer could have only carried these NLDs forward if it made the irrevocable Election as provided by the IITA, pertinent Regulation and IL-1120 form and checked the box below Part IV, Line 1 of its Returns. Taxpayer admits that it did not check the box and make the Election. Inasmuch as Illinois law does not provide a basis upon which one may be excused from the consequences of failing to opt for the Election, Taxpayer's statement that such failure was the mistake of Taxpayer's accountant does not absolve Taxpayer of the consequences of the failure to choose the Election. Taxpayer neither disputes the amounts the Department seeks in the NOD, nor the material and salient fact that Taxpayer failed to check the boxes on its Returns. Therefore, the Department properly amended Taxpayer's Return for the period ending November 2007 to carry back the NLD for the 2001 period to 1999 where it was completely utilized and carry forward the NLD for the 2002 period to the 2004 through 2006 years.<sup>2</sup> Mn. p. 3.

In light of the above, there is no genuine issue of material fact and the Department is entitled to judgment in its favor.

**Recommendation:**

For the reasons stated above, the Department's motion for Summary Judgment is granted and, as such, the NOD should be finalized, pursuant to statute.

September 28, 2010  
Date

Julie-April Montgomery  
Administrative Law Judge

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<sup>2</sup> This NLD could not be utilized in the year ending November 2000 because Taxpayer had a loss and, as such there was no income to be offset by the NLD. Mn. p. 3.