

IT 98-8

Tax Type: INCOME TAX
Issue: Withholding Tax - Failure to File Return/Make Payment
Non-Filer (Failure To File Returns - Extends Limit)

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

THE DEPARTMENT OF REVENUE
OF THE STATE OF ILLINOIS

v.

XYZ CO., INC.

No.
FEIN
1st Qtr. 1981

Mimi Brin
Administrative Law Judge

RECOMMENDATION FOR DISPOSITION

Appearances: Mr. James Harbert of Hinshaw & Culbertson, for XYZ CO., INC.; Mr. Sean Cullinan, Special Assistant Attorney General, for the Illinois Department of Revenue

Synopsis:

This matter comes on for hearing pursuant to the XYZ CO., INC.'s (hereinafter referred to as the "Taxpayer" or "XYZ") protest of a Notice of Deficiency (hereinafter referred to as the "NOD") by the Illinois Department of Revenue (hereinafter referred to as the "Department") proposing an assessment of tax based upon taxpayer's failure to file the necessary return (hereinafter referred to as the "IL-941") indicating the amount of employees' compensation it withheld for the 1st quarter of 1981, and taxpayer's failure to pay over to the Department those monies. The NOD also proposed penalties pursuant to sections 1001 and 1002(c)(1) of the Illinois Income Tax Act (35 ILCS 5/101 *et seq.*)

(hereinafter referred to as the “Act”). A hearing in this matter was held on May 28, 1998 whereat Ms. Deborah Rabbitt (hereinafter referred to as “Rabbitt”), the records manager of the central files area of the records management division of the Department, testified on behalf of the Department and JOHN DOE (hereinafter referred to as “DOE”) testified for the taxpayer.

At a pretrial conference, the parties agreed that the issues in this cause are whether the taxpayer filed and paid its withholding tax liability for the 1st quarter of 1981; whether the Department can issue this NOD beyond the statutory limitations period set forth in section 905(j) of the Act; and, whether sections 1001 and 1002(c)(1) penalties should be applied. Order, February 20, 1998

Following the submission of all evidence and a review of the record, it is recommended that this matter be resolved in favor of the taxpayer for both tax and penalties proposed. In support thereof, I make the following findings of fact and conclusions of law:

Findings of Fact:

1. The Department’s *prima facie* case, inclusive of all jurisdictional elements, is established by the admission into evidence of the Notice of Deficiency, dated April 17, 1995, proposing an assessment of tax, penalties and interest, to date of issue, of \$20,742.44, based upon taxpayer’s failure to file and pay employees’ withholding tax for the 1st quarter of 1981. Department Ex. No. 2

2. Department records for this taxpayer do not contain any filing or payment for this taxpayer of employees withholding tax return for the 1st quarter of 1981. Department Exs. Nos. 3, 5, 6
3. The Department received taxpayer's Reconciliation of Illinois Tax Withheld and Transmittal of Income and Tax Statements form (hereinafter referred to as the "IL-W-3") for the year ending 12/31/81, which included 281 W-2s and showed an amount of \$7613.22 as having been reported and paid by taxpayer for the 1st quarter of that year. Taxpayer Ex. No. 4; Tr. pp. 63-65
4. The amounts shown on the 1981 IL-W-3 as having been reported and paid to the Department for withholding taxes correspond to the cancelled checks for same reviewed by the preparer of that IL-W-3. Tr. p. 66
5. The Department did not maintain hard copy copies of withholding tax returns for the year 1981 beyond four years. Tr. pp. 42-43
6. There was a delay between receipt of withholding tax returns and the recording (hereinafter referred to as "recording", "processing" or "posting") of those returns onto the Department's computer system.
7. There were extraordinary delays in the recording of some of taxpayer's withholding tax returns filed during 1980 and 1981, with those delays set forth by the following:

Quarter	Date Received by Department	Date Processed by Department
1 st Quarter 1980	April 23, 1980	March 15, 1982
2 nd Quarter 1980	August 1, 1980	March 17, 1982

2 nd Quarter 1981	July 30, 1981	May 27, 1983
3 rd Quarter 1981	November 3, 1981	May 27, 1983
4 th Quarter 1981	February 3, 1982	April 10, 1982
1 st Quarter 1982	May 7, 1982	July 9, 1982
2 nd Quarter 1982	July 18, 1982	September 3, 1982
3 rd Quarter 1982	October 15, 1982	December 17, 1982
4 th Quarter 1982	January 18, 1983	March 16, 1983

Conclusions of Law:

The Illinois Income Tax Act directs, *inter alia*, that every employer in this State withhold a tax on compensation paid in this State (35 ILCS 5/701) and that the employer is to remit the withheld payments to the Department *via* quarter monthly returns and payments. 35 ILCS 5/704 Should the employer fail to file a necessary return, the Act provides, generally, that the Department may issue at any time (35 ILCS 905(c)) but, more specifically, the Act states:

(j) Withholding tax. In the case of returns required under Article 7 of this Act (with respect to any amounts withheld as tax or any amounts required to have been withheld as tax) a notice of deficiency shall be issued not later than 3 years after the 15th day of the 4th month following the close of the calendar year in which such withholding was required. (emphasis added)

35 ILCS 905(j)

The NOD at issue herein was issued on April 17, 1995, fourteen years after XYZ's withholding tax for the 1st quarter of 1981 was due to be filed and paid. The Department relies on section 905(c) to support the fourteen year lapse in issuance, whereas the taxpayer argues that the three year limitation period found in 905(j) dictates- thus, the NOD was not timely issued.

I do not agree with taxpayer's position, as I find that the language of 905(j) specifically provides a three year limitations period when the employer has failed to pay

the required withholding, as is clear from the emphasized language cited, *supra*, and that in the case, such as here, wherein the employer has failed to file a return, the legislature has not set any limitations period on the Department to issue the NOD.

However, this matter raises the question of whether this taxpayer did file the required return and pay the money due. On this issue, XYZ prevails.

The Act gives the NOD *prima facie* correctness and is “*prima facie* evidence of the correctness of the amount of tax and penalties due.” 35 ILCS 5/904(b) But, taxpayer argues, when the Department bases its notice upon the failure to file and, thereby, exceeds the ordinary limitations period for issuance, the Department is required to make an affirmative showing, as part of its *prima facie* case, that there was such a failure to file. Patrick Mitchell v. Department of Revenue, 230 Ill. App.3d 795 (1st Dist. 1992)

The Department did that, in the form of the affidavit of Deborah L. Rabbitt, records manager for the Department, which states that a search of Department records failed to show the processing of an Illinois Employers’ Quarterly Withholding Tax Return for March, 1981 Department Ex. No. 3.¹ Also made part of the Department’s *prima facie* case is a computer printout of the taxpayer’s withholding tax account for the quarters of 1981 and 1982, which shows that no IL-941 was filed for XYZ for the 1st quarter of 1981. The Department offered its exhibits under the Certification of Records signed by Ken Zehnder, Director of the Illinois Department of Revenue. Department Ex. No. 6

¹ Ms. Rabbitt, on cross-examination, testified that she, herself, did not conduct the examination of Department records on or before November 13, 1997, as stated on Exhibit 3. Tr. p. 45 However, she testified that she did search the Department’s records for taxpayer’s 1st quarter, 1981 filing after that date. Tr. pp. 45-51

XYZ objected to admitting the computer printout into evidence, relying on Grand Liquor Co., Inc. v. Department of Revenue, 67 Ill.2d 195 (1977), a case concerning the Retailers' Occupation Tax Act, Ill. Rev. Stat. 1973 ch. 120, par. 440 *et seq.*² Tr. pp. 22-25 In that case, the Department's correction of returns was based upon computer information of that taxpayer's records. The court did not allow those correction of returns *prima facie* correctness because the Department did not establish the reliability of that computer information.

At the time of Grand Liquor, the pertinent statutory provision gave *prima facie* correctness to the Department's determination of liability when submitted under the certificate of the Director of Revenue. Ill. Rev. Stat. 1973, ch. 120, par. 443 There was no provision for computer data or print-outs of Department records being given the same *prima facie* correctness. The Grand Liquor court, relying on a Mississippi supreme court case (King v. State ex rel. Murdock Acceptance Corp., 222 So.2d 393, 398 (1969)), determined that a foundation was necessary in order to give the Department's computer records *prima facie* correctness. The Illinois legislature addressed this situation by amending pertinent provisions (P.A. 83-1470, effective September 20, 1984) thereby providing that if computer data and print-outs are offered as proof of Department corrections, "the Director must certify that those computer print-outs are true and exact representations of records properly entered into standard electronic computing equipment, in the regular course of the Department's business, at or reasonably near the time of the occurrence of the facts recorded, from trustworthy and reliable information." 35 **ILCS** 120/4 The Illinois Income Tax Act, under which this case is determined, was, likewise, amended. 35 **ILCS** 5/914 (P.A. 85-299, effective September 9, 1987)

² The Retailers' Occupation Tax Act is now found at 35 **ILCS** 120/1 *et seq.*

Department Ex. No. 6, the certification of records objected to by taxpayer, contains the following language:

To the extent such documents or records included herein consist of computer generated data [sic], it is further certified that such information is a true and exact representation of records properly entered into standard electronic computer equipment in the regular course of the Department's business, at or reasonably near the time of occurrence of the facts recorded, from trustworthy and reliable information.

Therefore, pursuant to 35 ILCS 5/904 and 914, the computer print-out (Department Ex. No. 5) showing that XYZ did not file or pay withholding taxes for the 1st quarter of 1981 is admissible, without further foundation, and is given *prima facie* correctness as to that determination. 35 ILCS 5/904(b)

The question remains as to whether taxpayer rebutted the Department's *prima facie* showing that it failed to file and pay withholding tax for the 1st quarter of 1981. I find that XYZ has done so.

It is well settled in Illinois that following the admission into evidence of the Department's *prima facie* case, the burden of proof is placed upon the taxpayer to rebut it with credible evidence (Balla v. Department of Revenue, 96 Ill. App.3d 293 (1st Dist. 1981)), which must be more than oral testimony. *Id.*; A.R. Barnes & Co. v. Department of Revenue, 173 Ill. App.3d 826 (1st Dist. 1988) The evidence of record herein is that XYZ filed, and the Department received, its IL-W-3 (Reconciliation of Illinois Tax Withheld and Transmittal of Income Tax Statements) for the year 1981. That document provided that taxpayer reported and paid \$7,613.22 in withholding tax for the 1st quarter,

1981.³ The Department did not respond to this document after receiving it until the NOD issued almost fourteen years after the IL-W-3 was filed.

In addition to this documentary evidence, DOE, the preparer of the IL-W-3, testified, credibly, that he prepared it using XYZ's books and records, all of which were available to him at that time. Tr. p. 63 DOE prepared the IL-W-3 by reconciling taxpayer's W-2 forms with the IL-941 filed and with cancelled checks. Tr. p. 66 The documents that he used at the time to do the reconciliation and to prepare the IL-W-3 are no longer available, nor was he able to get the documents from the bank XYZ used at the time. Taxpayer Ex. Nos. 5, 6 Given the length of time that passed before the issuance of the NOD, the lack of greater documentation is not unreasonable. Given the totality of the evidence, XYZ, through testimony and documentation rebutted the *prima facie* correctness of the NOD.

The Department's position is that DOE's testimony and the IL-W-3 are not sufficient to rebut the NOD. The Department correctly argues that its records for this taxpayer appear accurate for all quarters prior and subsequent to the one at issue. Tr. pp. 91-92 However, this evidence presents some concern. There were lengthy time delays between the Department's receipt of XYZ's withholding tax returns for the 1st and 2nd quarters of 1980 and the 2nd and 3rd quarters of 1981 and the posting of them to the computer system. Findings of Fact No. 7 These delays appear to be atypical (*compare*, 4th quarter, 1981; 1st, 2nd, 3rd, 4th quarters, 1982) and it is reasonable to conclude from this evidence that the Department's processing system was experiencing problems with this account around the 1st quarter of 1981, the quarter at issue.

³ The NOD proposes an assessment of \$7500 in tax, with additional penalties and interest. Taxpayer reported payments totaling \$7613.22 for the period at issue. The basis for the NOD's proposed tax amount

As a result of all these factors, I conclude that the taxpayer rebutted the *prima facie* correctness of the NOD, and, that the Department failed to prove its contentions by a preponderance of the evidence thereafter. Balla v. Department of Revenue, *supra*

WHEREFORE, for the reasons stated above, it is my recommendation that the Notice of Deficiency issued to XYZ CO., INC., proposing an assessment of tax, penalties and interest based upon the failure of XYZ to file and pay withholding tax for the 1st quarter of 1981, be cancelled.

6/30/98

Mimi Brin
Administrative Law Judge

was never established.