

MF 04-8

Tax Type: Motor Fuel Use Tax

Issue: Reasonable Cause on Application of Penalties

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

THE DEPARTMENT OF REVENUE)	
OF THE STATE OF ILLINOIS)	
)	Docket No. 03-ST-0000
v.)	Acct # 0000000000
)	
ABC TRANSPORT CO.)	
)	
Taxpayer)	

RECOMMENDATION FOR DISPOSITION

Appearances: John T. Robinson, Special Assistant Attorney General, for the Department of Revenue of the State of Illinois; Andrew K. Light of Scopelitis, Garvin, Light & Hanson for ABC Transport Co.

Synopsis:

This case concerns whether a portion of the interest assessed against ABC Transport Company (“taxpayer”) in connection with its motor fuel tax liability under the International Fuel Tax Agreement (“IFTA”) may be abated. The Department of Revenue (“Department”) conducted an audit of the taxpayer for the period of January 1, 1999 through March 31, 2002. On August 16, 2002, the Department issued a Notice of Proposed Liability that proposed additional tax due as a result of the audit, plus interest and a penalty. After the Department’s notice was issued, several IFTA members made a formal request to the Department for a re-audit. The Department conducted a re-audit,

and on July 30, 2003 the Department issued a Notice of Proposed Liability that resulted in a net fuel tax reduction, no penalty, and interest that was calculated from January 1, 1999 through July 31, 2003.¹ The taxpayer has not challenged the Department's tax or interest calculations, but has filed a protest concerning the interest that accrued between the conclusion of the first audit and the second audit. The taxpayer refers to this as the "interim interest" and asks that it be abated because it would not have accrued if the Department had made the proper calculations at the close of the first audit. The parties have filed Motions for Summary Judgment, stipulations, and briefs in support of their motions. After reviewing the documents submitted by the parties, it is recommended that this matter be resolved in favor of the Department.

FINDINGS OF FACT:

1. The taxpayer is an authorized for-hire interstate motor carrier based in Anywhere, Illinois. (Stip. #8b)²
2. The taxpayer owns and/or leases commercial motor vehicles, which are based in Illinois. The taxpayer operates the commercial vehicles in Illinois and other IFTA-member jurisdictions. (Stip. #9, 13)
3. The State of Illinois imposes a motor fuel tax on fuel consumed by interstate commercial motor vehicles, and it participates in IFTA. (Stip. #10, 11)
4. The State of Illinois was and is an IFTA member jurisdiction and is subject to its Articles of Agreement. (Stip. #4)

¹ Although the second audit resulted in a net tax reduction, the taxpayer had overpaid its liability for some jurisdictions and underpaid its liability for others. Under IFTA, the interest is calculated separately for each jurisdiction. This resulted in an interest assessment for each jurisdiction for which the taxpayer underpaid its liability.

² Due to a typographical error, the stipulations are numbered incorrectly. After the paragraph numbered 7, there is another paragraph 5 and 6 and no paragraph 8. The "second" 5 and 6 paragraphs will be referred to as 8a and 8b.

5. The Department is an agency that is authorized to administer and enforce the Illinois IFTA program. (Stip. #14)

6. The taxpayer participates in the Illinois IFTA program. (Stip. #12)

7. The taxpayer filed quarterly motor fuel use tax returns with the Department for the period of January 1, 1999 through March 31, 2002. The Department conducted an audit of the taxpayer's motor fuel use tax records for this time period to verify motor fuel use tax liabilities to various jurisdictions in which the taxpayer's commercial motor vehicles operate. (Stip. #15, 16)

8. Pursuant to an agreement between the Department and the taxpayer, the auditor used the "error factors" for mileage that were used in a previous audit of the taxpayer. The previous audit covered the period of July 1, 1994 through September 30, 1997. The auditor used the error factors from the previous audit for purposes of saving time and expense for both parties. (Stip. #7; Ex. #5)

9. As a result of the initial audit, on August 16, 2002, the Department issued form EDA 123 Notice of Proposed Liability to the taxpayer that proposed additional tax in the amount of \$5,753, penalty of \$575.30, and interest of \$78,044.82 for a total assessment of \$84,373.12. (Stip. #17)

10. The taxpayer made an initial payment of \$6,328.20 for the tax and penalty assessed and protested the results of the audit. (Stip. #6, 18)

11. As a result of the first audit, miles and corresponding tax liabilities were re-allocated from some states to other states. For example, the auditor determined that the taxpayer owed Illinois \$125,701.34 and was due refunds from Indiana, Missouri, and Ohio in the amounts of \$99,880.83, \$36,042.72, and \$78,151.25 respectively. (Stip. #19)

12. Following the first audit, several IFTA-member jurisdictions, including Indiana, Missouri, and Ohio, made formal requests to the Department for a re-audit of the taxpayer's records. (Stip. #20)

13. The protesting jurisdictions objected to the Department's use of mileage error factors derived from the 1994-97 audit. They contended that the error factors were not representative of the taxpayer's business operations during the audit period. (Group Ex. #8)

14. The Department performed a re-audit and did so with the assistance of several out-of-state auditors. (Ex. #1)

15. After the re-audit, on July 30, 2003 the Department issued form EDA-123 Notice of Proposed Liability indicating the taxpayer was entitled to a net tax reduction of \$46,371.27. The Notice did not assess a penalty, but showed interest due in the amount of \$97,544.63 (as calculated from January 1, 1999 through July 31, 2003). (Stip. #23)

16. As a result of the re-audit, miles and corresponding tax liabilities were re-allocated again, but in amounts that differed significantly from the initial audit. For example, the Department determined that the taxpayer was entitled to a refund from Illinois and Indiana in the amounts of \$69,090.26 and \$33,033.42 respectively. Also, the Department determined that the taxpayer owed Missouri \$94,034.14 in tax, plus interest at the rate of 1% per month. (Stip. #24)

17. After giving the taxpayer credit for the \$6,328.30 payment made following the initial audit, the re-audit resulted in a net liability of \$44,845.06, all of which was interest. On August 4, 2003, the taxpayer paid this amount to the Department under protest. (Stip. #25, 26)

18. The liabilities that were assessed as a result of the re-audit accrued interest for the eleven-month period of August 2002 through July 2003. During this time period, the Department determined that the following interest amounts were owed to these jurisdictions:

Arkansas	\$ 1,413.52
Iowa	2,219.58
Michigan	1,955.19
Michigan-surcharge ³	2,606.92
Missouri	10,343.76
Ontario	311.35
Pennsylvania	6,780.79
Tennessee	2,676.77
Wisconsin	19.06
West Virginia	<u>2,722.71</u>
Total	\$31,049.65 (Stip. #28)

19. The taxpayer has solicited the Motor Fuel Tax Administrators in each of the above jurisdictions (except Arkansas, Ontario and Wisconsin) and asked that the interest be waived. The State of West Virginia has agreed to waive the interest in the amount of \$2,722.71. (Stip. #29)

CONCLUSIONS OF LAW:

The Articles of Agreement require audit interest to be calculated separately for each jurisdiction, and it accrues monthly until it is paid. Ex. 4, Article XII, ¶R1230.300.010. An overpayment for one jurisdiction has no effect on the interest calculation for any other jurisdiction. *Id.* The interest accrues at the rate of 1% per month. Ex. 4, Article XII, ¶R1230.100. The Articles of Agreement do not require any jurisdiction to pay interest to the taxpayer on overpayments.

Under the Articles of Agreement, a member jurisdiction may re-examine a base jurisdiction's audit findings if, within 45 days of receiving the audit report, it notifies the

³ This surcharge was not explained in the record.

base jurisdiction of any errors found during the review of the audit and of its intention to conduct the re-examination. Ex. 4, Article XIII, ¶R1360.100. The re-audit or re-examination by a member jurisdiction must be performed in cooperation with the base jurisdiction. Ex. 4, Article XIII, ¶R1360.300. An adjustment must be reconciled with the original audit findings, and new audit findings must be issued by the base jurisdiction. Id. A member jurisdiction conducting a re-audit or re-examination must pay its own expenses. Id.

Shortly after the initial audit was complete, various member jurisdictions objected to the initial audit, and the Department conducted a re-audit, which took 11 months. Because the taxpayer underpaid its motor fuel use tax liability in several jurisdictions, this resulted in an interest assessment in an amount of \$97,544.63 at the conclusion of the second audit.

The taxpayer had raised two arguments. First, the taxpayer contends that the Department should bear the cost of the \$31,049.65 of interim interest and refund this amount to the taxpayer. In the alternative, the taxpayer argues that the Department should pay the taxpayer interest at the rate of 1% per month on the \$69,090.26 that was overpaid to Illinois as determined by the second audit.⁴

The taxpayer believes that the Department should pay the interim interest because it is the cost associated with the Department's failure to follow proper IFTA audit procedures in the first audit. The taxpayer asserts that the Articles of Agreement do not preclude this result. The taxpayer states that nothing in the Articles of Agreement addresses who should bear the cost of the Department's failure to conduct a proper audit

⁴ At the time that the taxpayer's brief was submitted, the interest on the overpaid amount totaled approximately \$31,593.57, which coincidentally is approximately the same as the amount of the interim interest.

the first time, or who should bear the expense of the interim interest, which is essentially the cost of the Department's original failures. The taxpayer argues that nothing in the Articles of Agreement precludes the Department from being made to bear the expense of its own mistakes.

The taxpayer maintains that under Illinois law, the Department should bear the cost of the erroneous audit. According to the Illinois Taxpayer Bill of Rights, the Department has the duty "[t]o abate taxes and penalties assessed based upon erroneous written information or advice given by the Department." 20 ILCS 2520/4(c). The taxpayer claims that it was assessed additional interest as a result of the erroneous advice that the Department gave during the first audit. In the taxpayer's view, the Bill of Rights supports a finding that the Department is responsible for the interim interest.

In addition, the Bill of Rights states that the Department has the duty "[t]o pay interest to taxpayers who have made overpayments at the same rate as interest charged on underpayments." 20 ILCS 2520/4(h). The taxpayer asserts that the State of Illinois, like all IFTA jurisdictions, charges 1% on underpayments. The taxpayer maintains that the Department should pay the taxpayer 1% interest on the \$69,090.26 that the taxpayer overpaid to Illinois during the audit period.

The Department argues that pursuant to Article XII, ¶R1260 of the Articles of Agreement, Illinois must receive written approval from another jurisdiction to waive interest for that jurisdiction. Only West Virginia has agreed to waive the interest that accrued in this matter. The Department states that it has no authority to abate the interest without approval from the other jurisdictions.

The Department contends that the taxpayer is not entitled to interest on the overpayment to Illinois. The Department maintains that interest on overpayments cannot begin to accrue until the amount of the overpayment is established, and the overpayment amount was not established until the Department finished re-examining the taxpayer's books and records. Until the re-examination was complete, there was no basis upon which to calculate the amount of the taxpayer's overpayment. Even if there was a basis on which to calculate a refund, the Department argues that the overpayment must first be applied to amounts the taxpayer owes other jurisdictions. Credits and refunds will be made only when all motor fuel use tax liabilities owed to other jurisdictions have been satisfied. 86 Ill.Admin.Code §500.340. Under Illinois law, interest on overpayments does not begin to accrue until more than 90 days have elapsed since the taxpayer requests a refund that is determined to be properly due. Id.

Furthermore, the Department notes that the Articles of Agreement require taxpayers to maintain adequate records of miles traveled and fuel purchased and to pay to the base jurisdiction the proper tax. Ex. 4, Article 12, ¶R1230. Taxpayers are required to file quarterly returns setting forth the number of miles actually traveled in each jurisdiction and to pay the tax. Ex. 4, Article 9. The Department claims that if the taxpayer in this case had kept records of actual mileage, neither the initial audit nor the re-audit would have revealed hundreds of thousands of dollars of tax overpayments and underpayments based on faulty reporting of mileage. In the Department's view, it should not bear the burden of the taxpayer's own failure to maintain its records in accord with the IFTA requirements.

Finally, the Department maintains that it did not provide the taxpayer with erroneous written information or advice within the meaning of the Taxpayer's Bill of Rights. The Department notes that the taxpayer does not dispute the amount of the assessments for any jurisdiction, and the taxpayer does not assert that the Department erroneously advised it to overpay its tax liability. The Department claims that the taxpayer did not rely on written information or advice from the Department in determining its tax liability.

The Department's arguments are persuasive. The Bill of Rights requires the Department to "abate taxes and penalties assessed based upon erroneous written information or advice given by the Department." 20 ILCS 2520/4(c). First, the taxpayer has not requested that the Department abate the taxes or a penalty. The taxpayer has requested that the interest be abated, which is not referred to in the Bill of Rights. Also, the Department did not provide the taxpayer with erroneous written information or advice that resulted in an assessment. The assessment in this case resulted from a discrepancy in the number of miles reported by the taxpayer, which was in part due to the taxpayer's failure to maintain trip sheets. (Ex. #1) The taxpayer did not receive erroneous information or advice from the Department that the taxpayer relied upon in preparing its tax returns or making decisions concerning its tax liability.⁵

The Department should not have to "bear the cost" of the second audit by paying the interim interest to the taxpayer. Nothing in the Articles of Agreement provides a basis for requiring the Department to pay the interim interest, and the taxpayer has not

⁵ From the stipulations it appears that the only error that occurred during the first audit was the use of the wrong error factors. The taxpayer agreed to the use of these factors. (Ex. #5) Although the taxpayer states that it did not in any way agree to "an improper audit" or waive any challenge to the audit, it still consented to the use of the error factors that were the cause of the improper audit.

presented a compelling reason for doing so. The mistake that occurred was a byproduct of the taxpayer's failure to maintain proper records, and the "cost" of that mistake cannot be attributed to the Department.

In addition, at this time the Department cannot be required to pay the taxpayer interest on the overpayment that the taxpayer made to Illinois. The Department's regulation concerning credits and refunds states that for IFTA licensees, the licensee may apply the overpayment that was generated in one jurisdiction to the taxes owed to another jurisdiction. 86 Ill.Admin.Code §500.340(a). "Credits and refunds will be made only when all tax liability, including audit assessments, has been paid to the Department or when all motor fuel use tax liabilities, including audit assessments, penalty and interest owed to other jurisdictions, has been satisfied." 86 Ill.Admin.Code §500.340(c). "Refunds determined to be properly due shall be paid within 90 days after receipt of a request by the licensee. If not so paid, interest shall accrue at the rate of 1 percent per month or fraction thereof until the refund is paid." 86 Ill.Admin.Code §500.340(e).

The taxpayer's overpayment to Illinois was applied to the taxpayer's motor fuel use tax liability that was owed to other jurisdictions. Because the overpayment was applied to other liabilities, the taxpayer has not specifically requested a refund. If the taxpayer had requested a refund, and if it was established that a refund was properly due to the taxpayer, and if the Department did not pay the refund within 90 days after receipt of the request, then interest would accrue at the rate of 1 percent per month or fraction thereof. None of these conditions have been met in this case.

Recommendation:

For the foregoing reasons, it is recommended that the Department's Motion for Summary Judgment be granted and the taxpayer's Motion for Summary Judgment be denied. Because the State of West Virginia has agreed to waive its share of the interest, that portion will be abated.

Linda Olivero
Administrative Law Judge

Enter: November 22, 2004