



ILLINOIS AUDIT SESSION

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Rules for this Session:

- (1) Confidential Exchange of Information
- (2) No Federal/State/Local Government Presence
- (3) Resolution/Follow Up

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Tips / Best Practices – Pre-Audit

- Plan ahead – understand whether taxpayer has issues that cannot be settled at audit will help shape audit strategy
- Maintain contemporaneous documentation for major transactions and significant state tax positions (Facts and legal analysis)
- Consult advisor / legal counsel in early stages for advice on audit strategy for significant issues

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Tips / Best Practices – Initial Meetings with Auditor

- Establish scope of audit
- Require that all audit requests for information and questions be in writing and agree on time frame for responding to information documentation requests (IDRs)
- Determine auditor plans to be on-site and establish opening audit guidelines in advance – e.g., standard office hours, office security, audit contact at company, requesting concluding conference, copies of workpapers
- Consider establishing portal for sharing documents

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Tips / Best Practices – During the Audit

- Be cooperative and timely respond to audit requests
- Keep records of all communication between taxpayer and auditor
- Schedule face-to-face meetings / check-ins with auditors and/or supervisors to gauge how audit is progressing and how Department feels about taxpayer positions (opportunity to deal with factual misconceptions)

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Tips / Best Practices – Information Requests

- Auditor may request more data than necessary to address an issue (ex. copies of all state returns, etc.)
- Understand why auditor is requesting information to ensure data being provided is most suitable to address question (prevent wasting time gathering excessive information)
- Maintain open dialogue with auditor to facilitate understanding why certain items are being requested and offer appropriate alternatives

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Tips / Best Practices – Statute Waivers

- Consider all facts and circumstances prior to signing a statute waiver
- Consider strategy to delay audit to more convenient time and give taxpayer time to locate requested information not readily available
- Provide time for taxpayer to review for offsetting refunds or credits to reduce potential assessment
- Limit potential for auditor to issue aggressive assessment when pressed for time
- Consider negotiating the length of the waiver

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1. Audit Rotation – Income Tax

A Fortune 100 company was advised by its IDOR auditor that if the audit did not generate a \$500,000 assessment, the company would drop from audit rotation.

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2. ICB Review

Rejection for improper documentation? Letter accepting request reminds taxpayer that 86 Ill. Admin. Code 215.115 requires inclusion of all supporting documentation with ICB-1; letter gives taxpayer 20 days to make any additional submission.

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3. Sales Tax – Resale Certificates

IDOR auditors refusing to accept alternative proof of a sale for resale; requiring a resale certificate. 86 Ill. Admin. Code 130.210(c) requires active registration numbers or active resale number from IDOR and “a certification” that the sale is for resale.

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4. Auditor Communication Issues

Auditors being generally reluctant to discuss basis for assessing tax; referring taxpayers to spreadsheets/indecipherable notes instead of engaging in a conversation.

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5. Income Tax / Bonus Depreciation

IDOR changing method of computation every audit cycle; refusing to start with computation from prior cycle. Also going back to closed, previously audited years and recomputing based on a new DOR template.

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6. Income Tax / R&D Credits

IDOR refusing to accept IRS workpapers or adjustments. Reviewing supporting documents and rejecting the R&D studies that have been completed and accepted for federal tax purposes.

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7. Tax Tribunal

- Endless IDOR extensions
- IDOR – favorable rulings

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8. Protest Act Litigation

- Sangamon County – Judicial assignment system
- Cook County
 - Separation of miscellaneous remedies from tax issues?

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9. Lease Transaction Tax Updates

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10. Delays

- Repeated long delays in responses from the Department, ICB, ALJs
- Second audits starting while first audit is still in ICB; ICB unwilling/unable to stay second audit pending its review.

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Recurrent Taxpayer Non-Compliance Issues – Sales Tax (from IDOR Website): Remote Retailer and Marketplace Facilitator Issues

- Leveling the Playing Field for Illinois Retail Act
- Taxpayers reporting UT instead of ROT
- Questionable nexus claims in attempt to qualify as out-of-state sellers only required to collect UT
- Marketplace facilitators not providing marketplace sellers with certification notifying them of collecting and remitting tax
- Insufficient documentation by remote retailers and marketplace facilitators to allow for verification of correct location of sale for purposes of verifying tax rate

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Recurrent Taxpayer Non-Compliance Issues – Sales Tax (from IDOR Website):

- Cash business issues
 - Compliance issues at cash businesses (bars, restaurants, liquor stores, convenience stores, gas stations)
 - Failure to keep or produce sufficient records to verify taxable sales

- Exemption documentation issues
 - Failure to obtain or maintain exemption documentation
 - Leads to delays in completing audits as taxpayers must gather documentation after audit has commenced

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Recurrent Taxpayer Non-Compliance Issues – Sales Tax (from IDOR Website):

- International Fuel Tax Agreement (IFTA) Issues
 - Failure to keep or produce the documentation to verify amounts claimed on returns
 - Failure to maintain logs to support miles driven
 - Failure to maintain purchase receipts
 - Failure to track fuel withdrawn from bulk

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Recurrent Taxpayer Non-Compliance Issues – Sales Tax (from IDOR Website):

- Transactional Return Issues
 - Compliance issues related to purchase of aircraft, watercraft, and vehicles
 - Rolling stock exemption on non-qualifying vehicles
 - Illinois residents purchasing vehicles from Illinois dealers claiming exemption for out-of-state residents from reciprocal states
 - Taxpayers claiming farm machinery and equipment exemption on equipment which frequently do not qualify for exemption (ex. ATVs, UTV, mowers) – failure to keep usage logs to support exempt usage
 - Purchases of watercraft from private parties at list price below actual purchase price
 - Failure to file/ pay use tax for aircraft hangered or primarily used in Illinois

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Recurrent Taxpayer Non-Compliance Issues – Income Tax (from IDOR Website):

– Apportionment Issues

- Taxpayers failing to correctly report numerator and denominator of apportionment factor resulting in smaller apportionment of income to Illinois
- Taxpayers not including receipts from sales of tangible personal property shipped to states where taxpayer is not taxable
- Taxpayers not including sales of services received in Illinois
- Improper inclusion of items in the denominator of receipts factor including foreign dividends, tax exempt interest, other items, subtracted as part of computation of base income

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Recurrent Taxpayer Non-Compliance Issues – Income Tax (from IDOR Website):

- Personal Service Income / Reasonable Compensation
 - Improper subtraction amounts for personal service income (PSI) or reasonable allowance for compensation paid to partners
 - Taxpayers using subtraction to zero out taxable income and eliminate replacement tax liability
 - Failure to maintain proper documentation to substantiate subtraction amount reported

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Recurrent Taxpayer Non-Compliance Issues – Income Tax (from IDOR Website):

– Bonus Depreciation

- Taxpayers not properly calculating addition and subtraction modifications for bonus depreciation
- Taxpayers keeping separate calculations for state and federal depreciation used for multi-state purposes and not specifically adhering to the more complex calculations required under Illinois law
- Taxpayers just plugging figures into the IL-4562

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Recurrent Taxpayer Non-Compliance Issues – Income Tax (from IDOR Website):

- Schedule E / Schedule C (Hobby Losses)
 - Taxpayers improperly reporting income and expenses on Schedule C or Schedule E
 - Taxpayers using hobby losses to reduce overall liability with no business they intend to run for a profit
 - Taxpayers under-reporting income related to business activities
 - Taxpayers over-reporting expenses and claiming wage expenses for which withholding not being paid
 - Schedule E audits – rental income and property expenses – family rentals

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Recurrent Taxpayer Non-Compliance Issues – Income Tax (from IDOR Website):

- Replacement Tax Investment Credit
 - Taxpayers improperly claiming credit that are not primarily engaged in qualifying activity to claim replacement credit
 - Taxpayers improperly claiming credit on non-qualified property
 - Taxpayers failing to report recapture credits for disqualified property

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New IDOR Publications:

- 8/20/24 FY 2025 – Estimate for Personal Property Replacement Tax
- 7/23/24 FY Bulletin 2025-01 – Guidance for Corporations Affected by Changes to Net Loss Deduction Limitation for Tax Years Ending On or After 12/31/24
- 6/26/24 FY 2024-29 – Hotel Operators' Occupation Tax Updates to Operators and Re-Renters of Hotel Rooms
- 6/4/24 Compliance Alert – Sales Made to Medicare Administrative Contractors



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