IT 14-0001 PLR 4/24/2014 TAXABLE YEAR
Taxpayer required to use two short taxable years for federal income tax purposes, but whose taxable year is otherwise unchanged and whose Illinois liability for the two short years would be the same as for a single tax year containing both short tax years, may file a single Illinois return for the tax year containing both short tax years.

April 24, 2014

Re: Company

Dear Xxxxx:

This is in response to your letter dated December, 2013, in which you request a Private Letter Ruling (PLR) on behalf of Company
Review of your request for a Private Letter Ruling indicates that all information described in paragraphs 1 through 8 of subsection (b) of 2 Ill. Adm. Code 1200.110 is contained in your request. This Private Letter Ruling will bind the Department only with respect to the combined group that includes Company
Issuance of this ruling is conditioned upon the understanding that Company
, the members of its combined group, and/or any related taxpayer(s) is not currently under audit or involved in litigation concerning the issues that are the subject of this ruling request.

The facts and analysis as you have presented them are as follows:

Company 2 is submitting this request for a Private Letter Ruling ("PLR"), pursuant to the provisions of Ill. Admin. Code tit. 2, § 1200.110 on behalf of our client Company,
seeking written confirmation from the Illinois Department of Revenue ("Department") upon which our client may affirmatively rely that either:

(1) Method 1. Notwithstanding that one entity in the Illinois combined filing group will be required to file two federal short-year income tax returns Company, along with the members of its Illinois combined filing group, may file, on or before July 15, 2014, one combined income and replacement tax return that covers the period from April 1, 2013 to March 31, 2014;

(2) Method 2. For the period beginning April 1, 2013, and ending March 31, 2014, despite being unitary with members that are included in the combined filing group, Company is not required to be included in the combined filing group for the purposes of the Illinois corporate income and replacement tax return covering that period.

We are requesting this ruling for the tax period commencing with the 2013 tax year only.

While the Department has issued guidance and letter rulings regarding the filing obligations following a federal short-year, we are unaware of any Illinois judicial or administrative rulings that have dealt directly with facts similar to those provided below.

To the best of Company and our knowledge, neither Company nor any of its affiliated companies is subject to any pending audit or litigation in Illinois involving the issues raised in this PLR request. To the best of Company's and our knowledge, the Department has not previously ruled on this issue for Company. No request for a ruling on the issues raised herein or similar issues have been submitted to the Department, and none has been withdrawn on behalf of Company or its affiliates. A power of attorney authorizing our representation of Company in this matter is attached.

Relevant Facts

Company is a member of a unitary business group that files an Illinois combined corporate income and replacement tax return (the "combined group"). Prior to the reorganization that is discussed, infra, the lead filer and designated agent of the combined group was Company 3. Company 3 operates in the U.S. as a branch of a foreign bank and files a Form 1120F for federal tax purposes. One other entity in the combined group files a separate federal Form 1120, while the remaining entities file a consolidated federal Form 1120. All of the entities are financial organizations under the Illinois income tax rules.

The Illinois combined group includes corporations with different tax years. Company 3, the lead filer, and the entity that files a separate federal Form 1120 have a tax year that ends on March 31. The other entities in the Illinois combined group are all calendar year taxpayers. The Illinois combined group has adopted the fiscal year of its lead filer – April 1 to March 31.

The Illinois fiscal year combined return includes the April 1st to March 31st taxable income/loss for the two fiscal year taxpayers and includes the taxable income/loss for the calendar year members whose tax year ends within the March 31 fiscal year of Company 3. For example, the Illinois combined tax return for the fiscal year ended March 31, 2013 includes the taxable income/losses for the two fiscal taxpayers and also the taxable income/losses for the other members' year ended December 31, 2012.

On June 30, 2013, Company 3 merged with an affiliated Country retail bank Company 4 which is not doing business in the United States, and then changed its name to Company, becoming the Company entity discussed herein. Under the Internal Revenue Code, a name change generally qualifies as a "Type F" reorganization; "a mere change is identity, form, or place of organization of one corporation, however effected." I.R.C. § 368(a)(1)(F). This was such a tax-free reorganization. As a result of the reorganization Company is the named lead filer and designated agent of the combined group.

Although this was a "Type F" tax-free reorganization, since Company
was a foreign corporation, its mere change in identity, form, or place of organization is deemed federally to be an asset transfer and close of the tax year, effective on the date of the close of the transfer. Treas. Reg. § 1.367(b)-2(f). Accordingly, for federal purposes, Company must file two short-year tax returns: one for the period April 1, 2013 to June 30, 2013, and one for the period July 1, 2013 to March 31, 2014

Legal Analysis and Authorities

The issue giving rise to this PLR request is that, without the relief being sought, there is no way to address the practical problems that would be associated with reporting, reviewing, and potentially auditing an Illinois combined corporate income and replacement tax return for which there is not corresponding federal returns for a majority of the members included in the combined group. As will be discussed, Illinois' mix of conformance and non-conformance to federal rules creates a situation in which a majority of the members of the Illinois combined group are required to be included in a short-year return for Illinois purposes, yet have no filing obligation for federal purposes. Such a situation presents bookkeeping, information gathering, and accuracy-related problems. As well, this situation limits the Department's ability to review and potentially audit the information that is reported.

In this request, the taxpayer is proposing to either (1) file a single Illinois combined return for the entire combined group at a time that coincides with the majority of the federal returns (proposed "Method 1"); or (2) remove from the combined group the member who has a federal short-year obligation so that just that member, and not the entire combined group, is obligated to file two short-year Illinois returns (proposed Method 2"). In either case, the result would be corresponding Illinois and federal income tax returns. Neither case would result in materially different tax consequences than would be the case if no relief is granted.

Federal Tax Law

The federal regulations create the short-year filing obligations for Company despite what is generally a non-event for tax purposes. A Type F reorganization is a "mere change in identity, form or place of organization of one corporation, however (a)ffected[.]" I.R.C. § 368(a)(1)(F). Provided that certain continuity and other caveats are satisfied, this type of reorganization is generally a non-event for federal tax purposes. See Treas. Reg. § 1.368-1(c). But, where the transferor corporation is a foreign corporation, there is a deemed asset transfer of the transferor's assets to the surviving corporation and the surviving corporation's taxable year is closed on the date of the transfer. Treas. Reg. § 1.367(b)-2(f)(1), (2). In this case Company is the surviving corporation, Company 3 was the transferor. Company 3 was a foreign corporation with operations in the United States. Pursuant to Treas. Reg. § 1.367(b)-2(f), Company 3 transferred its assets to Company on June 30, 2013, and, on that day, Company closed its tax year.

Company was required to close its tax year on June 30, 2013, but none of the other members of its unitary business group were required to do so. Prior to the transfer, Company was not doing business in the United States, and so it did have a U.S. income tax filing obligation; it was not included in any federal consolidated filing. For federal tax purposes, the transaction between Company 3 and Company had no effect on the entirely removed unitary companies. So, while Company was required to close its tax year on the date of the transfer, none of the other members of the Illinois unitary business group were required to close their tax years for federal tax return purposes.

Illinois Tax Law

In Illinois, corporations are required to file income tax returns "on or before the 15th day of the third month following the close of the tax year…" unless the federal return has a later due date, in which case the Illinois return is due on that later date. 35 Ill. Comp. Stat. 5/505(a)(1). The Illinois tax year is the same as the federal tax year. 35 Ill. Comp. Stat. 5/1501(a)(23); 35 Ill. Comp. Stat. 5/203(b)(1). When an income tax return is due to the federal government, one is also due to the State of Illinois.

Under federal law, Company must file two short-year returns. As discussed, *supra*, Treasury Regulation § 1.367(b)-2(f) created a short-year for Company ending on June 30, 2013, as the result of a deemed transaction. Then, to report the remainder of its fiscal year, Company is required to file a second short-year return covering the period from July 1, 2013 to March 31, 2014. The same is true for Illinois purposes. The federal tax year for the other members of the unitary business group were not impacted by the reorganization, and therefore, these members do not have short years.

The heart of the issue lies in Illinois' mandatory combined filing requirements. Company concedes that it is unitary with all of the other aforementioned entities, as it and the entities are "related through common ownership" and their "business activities are integrated with,

dependent upon and contribute to each other." See 35 Ill. Comp. Stat. 1501(a)(27). Accordingly, Illinois requires that these entities be treated as one taxpayer, and must file one combined Form 1120 with a Schedule UB. Ill. Admin. Code tit. 86, § 100.5210(b)(1), (2).

The problem is that Company's federal short year, while an isolated filing obligation for federal purposes, has now been imputed onto all of the other unitary business group members for Illinois purposes. Effectively, this has caused a disconnect between the federal tax year end and the Illinois tax year end for a majority of the members in the Illinois combined group. For federal tax purposes, the federal consolidated filing group closes its books and its tax year on December 31, 2013 and the federal form 1120F filer closes its books and its tax year on March 31, 2014. For Illinois purposes only, these entities must now close its books and records for a short period 2013 tax year on June 30, 2013. Having different federal and Illinois tax year ends creates a host of practical problems that can only be resolved by granting the relief that is being sought.

Company has submitted two alternative requests. The first request ("Method 1") is for Company to be permitted to file one full year Illinois corporate income and replacement tax return for the entire unitary business group to cover both of Company's short years, the federal fiscal year filers' entire fiscal year ending March 31, 2014, and the calendar year filers' entire tax year ending December 31, 2013. This return would have an original due date of June 15, 2014.

In the alternative, Company's second request ("Method 2") permits Company to be removed from the unitary business group for its federal tax years ending June 30, 2013 and March 31, 2014. This would allow Company to file two separate company Illinois corporate income and replacement tax returns to correspond with each of the two federal short-years. It would also permit the remaining members of the unitary business group to continue to file just as they historically have been filing. For the tax year ending March 31, 2014, these members would file one combined Illinois corporate income and replacement tax return.

There are three reasons why the Department should grant one of Company's requests. First, granting the request significantly limits an unnecessary burden on the taxpayer. For federal tax purposes, Company closed its books on June 30, 2013. None of the other unitary business group members did so. Under Illinois law, without relief, these other unitary business group members would have to prepare a short-year return for the short-year ending June 30, 2013 without actually having closed their books. Without the relief being sought, these companies would need to go back in time and have a soft closing of its books on June 30, 2013, calculate Schedule M adjustments specifically for each short period, and apportionment factor data as if they has closed their books. From an information gathering point of view, such a task would be daunting. Data would need to be gathered from internal business segments – not as of a natural point in time as would be the uniform end of a fiscal year – but at what would seem like an otherwise arbitrary point in time.

Likely, this process would result in a significant amount of estimates being used. It invites inaccuracies and would unnecessarily expose the taxpayer to a higher level of risk. This risk of inaccuracy and approximation, as well as the information gathering challenge, would be minimized by either of the taxpayer's proposals. Method 1 would permit one combined filing when the books are closed for federal tax purposes at the end of the fiscal year. Method 2 would allow Company to separate from the unitary business group, thus allowing it to report its own data from its own book closing date, while allowing the others to report their own data without having to create pro-forma short period returns.

The burden is equally imposed on the Illinois Department of Revenue should two short-year combined returns be filed. The Department would receive a combined return for the tax year ending June 30, 2013. It would be able to verify Company's information against Company's federal filing for the same short-year. But, for the remaining members of the unitary business group, there would be no federal short-year filing against which the reported information could be verified. Even once the remaining member's books are closed, it would not be possible to verify which portion of the federal filing is attributable to pre-June 30 and which is attributable to post-June 30.

Should the State decide to audit these tax years, the same information gathering and information verification problems would exist. Since the majority of the Illinois combined group members will not close their books on June 30, 2013, there would be the issue of attempting to determine whether apportionment data or income was properly attributed to pre- or post-June 30. The auditor would not be able to verify this information against a closed trial balance because the trial balance was not closed on that date. The auditor would not be able to verify this information against a federal return filing because there would not be one. Likely, there would not be any method to determine true accuracy; the only way an auditor would be able to determine whether apportionment data or income was properly attributed to the correct short-year would be to judge on a scale of reasonableness. Both proposed methods alleviate these issues by allowing for corresponding trial balance with Illinois and federal tax return filing obligations.

Finally, neither Method 1 nor Method 2 would distort the overall tax liability to the State. These methods are simply requesting that income be reported for different companies at different times so that the Illinois reporting periods and the federal reporting periods coincide for all of the companies. Under Method 1, all of the taxable income and apportionment data that would be included in the two short-year combined filings would be summed up and included in the single combined tax return. Under Method 2, Company's taxable income and apportionment data would be removed from the combined group filing. However, Illinois uses flat income and replacement tax rates, and so whether that apportioned income is included in the combined filing or taxed separately should not materially distort the overall amount of tax due.

Both Method 1 and 2 allow taxpayers to compute income for both federal and Illinois purposes using the same data. As well, it allows the Department the ability to easily verify that the data that is being reported is being reported consistently and accurately. In this situation, the interplay between the federal deemed transactions rules and the Illinois mandatory combined filing rules for unitary business groups goes against these purposes. Because either Method 1 or Method 2 would ease the burden on both the taxpayer and the Department, and because neither method would result in a materially different tax liability than would be computed under current law, the taxpayer requests that the Department grant its request for written confirmation.

For the reasons discussed above, we believe that we have exceeded the burden of proof and respectfully request that the Department provide the written rulings requested. If the Department intends to issue responses to the request that do not agree with the ruling position requested, we request that the Department contact us prior to issuing such a ruling in order to give us the opportunity to discuss the issue further and possibly request the opportunity to withdraw this request without the Department ruling.

In addition, we request that the identity of Company and the other parties described herein be redacted from any published version of a PLR that the Department does issue to Company.

RULING

Section 401(a) of the Illinois Income Tax Act (the "IITA" : 35 ILCS 5/101 *et seq.*) provides:

> For purposes of the tax imposed by this Act, the taxable year of a person shall be the same as the taxable year of such person for federal income tax purposes.

Section 401(b) of the IITA provides that, if any taxpayer has its federal taxable year changed, its taxable year for Illinois income tax purposes is also changed.

Department Regulations Section 100.5201(e) provides that, in the case of a combined group, the "common taxable year" means the taxable year used by the combined group in reporting its combined net income, as determined under the provisions of Section 100.5265. Regulations Section 100.5265 provides that the common taxable year of a combined group shall be the taxable year of the designated agent.

Treasury Regulation Section 1.367(b)-2(f)(4) provides:

> In a reorganization described in paragraph (f)(1) of this section, the taxable year of the foreign transferor corporation shall end with the close of the date of the transfer and, except as otherwise required under the Internal Revenue Code (e.g. section 1502 and the regulations there under), the taxable year of the acquiring corporation shall end with the close of the date on which the transferor's taxable year would have ended but for the occurrence of the reorganization if –
> (i) The acquiring corporation is a domestic corporation; or
> (ii) The foreign transferor corporation has effectively connected earnings and profits (as defined in section 884(d)) or accumulated effectively connected earnings and profits (as defined in section 884(b)(2)(B)(ii)).

Pursuant to this provision, the taxable year of Company beginning April 1, 2013 was terminated on June 30, 2013 as a result of its merger into Company in a transaction treated as a reorganization under IRC Section 368(a)(1)(F). Likewise, the taxable year of Company ends March 31, 2014. Pursuant to IITA Section 401(b) and Department Regulations Section 100.5265, the common taxable year of the Illinois combined group that includes Company is divided into two short taxable years, with one ending June 30, 2013 and the other ending March 31, 2014.

Nevertheless, in situations similar to the current situation, where one taxpayer is required for federal income tax purposes to divide its otherwise unchanged taxable year into two short taxable years because it is acquired by another corporation, and the taxpayer is not being added to the unitary business group of the acquiring corporation, the Department has ruled that the corporation may file a single Illinois income tax return for the entire 12-month taxable year rather than for the two short taxable years. See IT 87-0003 (January 5, 1987); IT 87-0025 (February 13, 1987); IT 87-0276 (November 5, 1987); IT 88-213 (July 22, 1987); and IT 2001-0034 (March 23, 2001).

Pursuant to those letter rulings, Company and its unitary business group may file a single Illinois combined income tax return for the common taxable year ending March 31, 2014. It must include in that return its tax items for its federal taxable years ending June 30, 2013 and March 31, 2014, the tax items of its member filing a separate federal form 1120 for its taxable year ending March 31, 2014, and the tax items of its remaining members for their taxable year ending December 31, 2013. The return shall have an original due date of June 15, 2014.

This ruling shall bind the Department for the common taxable year of the Company combined group ending March 31, 2014. The facts upon which this ruling is based are subject to review by the Department during the course of any audit, investigation or hearing and this ruling shall bind the Department only if the material facts as recited in this ruling are correct and complete. This ruling will cease to bind the Department if there is a pertinent change in statutory law, case law, rules or in the material facts recited in this ruling.

Sincerely,

Brian L. Stocker
Chairman, PLR Committee (Income Tax)