**No. 129562**

# In the Supreme Court of Illinois

MARATHON PETROLEUM COMPANY LP f/k/a
MARATHON PETROLEUM COMPANY, LLC,

*Plaintiff-Appellant/*
*Cross-Appellee,*

v.

COUNTY OF COOK, COOK COUNTY DEPARTMENT OF REVENUE, et al.,

*Defendants-Appellees/*
*Cross-Appellants.*

On Appeal from the Illinois Appellate Court, First Judicial District, No. 1-21-0635.
There Heard on Appeal from the Circuit Court of Cook County, Illinois,
County Department, Tax & Miscellaneous Remedies Section, No. 2019 L 050614.
The Honorable John J. Curry, Judge Presiding.

## APPELLANT'S REPLY BRIEF AND RESPONSE TO REQUEST FOR CROSS-RELIEF

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## ARGUMENT

The County's brief raises several unsuccessful arguments in defense of its imposition of Motor Fuel Tax ("Tax") on Marathon's Book Out transactions. The County begins by mischaracterizing this appeal as raising a question of fact rather than law. This effort fails; Marathon proved, and both the circuit and appellate courts agreed, that the transactions at issue are Book Out transactions. The County then raises a series of arguments to support its legal assertion that the Tax applies. These arguments are equally misguided, as the Book Outs did not involve a retail sale or a "sale" of any recognized nature under the Ordinance. The County's arguments that its interpretation of the Ordinance does not render the tax an unconstitutional occupation tax on Marathon with an improper extraterritorial effect are similarly unavailing because the County seeks to impose the Tax on financial transactions with no connection to Cook County. Finally, the County's cross claim for the reinstitution of the penalty charges set aside by the appellate court fails because it relies on an erroneous standard of proof, misconstrues applicable authority, and ignores the evidence of Marathon's reasonable tax position.

For all the foregoing reasons and as discussed in more detail below, the County's arguments should be rejected. The Book Out transactions are not subject to Tax under the plain language of the Ordinance and, even if this Court finds ambiguity, binding precedent requires that the Ordinance be construed in Marathon's favor. In any event, the penalties were properly abated by the appellate court.

### I. Marathon Proved that the Transactions at Issue are Book Out Transactions.

The central premise of the County's brief is that Marathon failed to offer books and records proving that the transactions at issue are Book Outs. This erroneous

assertion underlies every argument the County raised in its brief. *See, e.g.*, County's Br. at 22-33, 44, 49, 58, 61. It is the basis for the County's contention that this appeal raises only a question of fact subject to a clearly erroneous standard of review. County's Br. at 22. The County is so committed to this fallacy that it failed to make any other response to many of Marathon's arguments and made no response to any of the arguments advanced in the four separate briefs filed by the amici. The County is undaunted by the fact that *both* reviewing courts found no such failure of proof. The circuit court explained in depth the documentary and testimonial evidence that firmly established the transactions at issue are Book Out transactions. *See, e.g.*, A-65-78. The appellate court agreed with the circuit court, finding that "[t]he question here is not whether book-out transactions occurred, but how forward contracts with corresponding book-out transactions should be treated for tax purposes." A-11.

Contrary to the County's repeated assertion, the record is clear that Marathon proved, via its books and records and supporting witness testimony, that the transactions at issue are Book Outs.

### A. The record is clear that the transactions at issue are Book Outs

The Marathon business record that unequivocally establishes the occurrence of the Book Out transactions is Marathon's Internal Summary Report, or "ISR." *See* C8244-8304. The ISR is a spreadsheet listing transactions with columns indicating the motor fuel buyer, invoice dates and numbers, quantities purchased (net gallons of fuel), origin and destination names. *Id*. All of the Book Out transactions at issue are clearly identified on the ISR, labeled as "Book Transfer" in the "Carrier" column. Contrary to the County's assertion that Marathon did not quantify the number of distressed contracts

at issue, the ISR identifies every Book Out at issue. *See* County's Br. at 10-11. Personnel at Marathon used the terms "Book Transfers" and "Book Outs" interchangeably. C 10616, 10618. All of the Book Out transactions had "Chicago IL" in both the origin and destination columns. C 8244-8304. Marathon witness Joseph Steiner explained that because of limitations in Marathon's computerized accounting system, Marathon was required to use the same format for Book Out transactions as it used for product sales, thereby resulting in the company placing "book transfer" as an entry under "Carrier," and "Chicago IL," in both the origin and destination column. C 12696-97. Mr. Steiner also testified that the term "Chicago IL" entered on the ISR for origin and destination was not a geographic term for the delivery or transfer of Motor Fuel but was an indicator for the pricing of the product and "Chicago IL" referred to the Chicago pricing region, one of several in the United States. C 12683. His testimony is buttressed by the fact that Marathon had no Chicago terminal or facility for the storage and sale of Motor Fuel. C 12452, 12513-14.[1]

Mr. Steiner testified that "a book out transaction is a mechanism which is used to settle contracts and to remove associated obligations without physically moving or transferring any product." C 12681. Marathon witness Matthew Freeman, a Marathon commercial analysis manager with significant knowledge of Marathon's financial settlements, testified that when Marathon settles a forward contract with a buyer through a cash settlement (a Book Out) no motor fuel is physically transferred, moved, or delivered. C 12476, 12496-97. He further testified that a Book Out involves no change of possessory rights or title to motor fuel. *Id*. Mr. Freeman testified that the cash

[1] Contrary to the County's allegation, Marathon's documents reflect no intentional failure to keep accurate books and records. *See* County's Br. at 30.

settlement or Book Out is merely "an accounting exercise." C 12476.

The County has no real argument that Marathon cannot rely on the ISR to establish that the transactions at issue are Book Out transactions as it wholly relied on that very same document in generating the Revised Assessments. The ISR was introduced into evidence by the County as Petitioner's Exhibit 1. C 8244-8304, 11385. The County's auditor testified that the County relied on the list of the transactions on the ISR to determine which transactions should be subject to Tax. C 11387-89. He testified that the County assessed Tax against Marathon for every purchaser on the ISR that was an unregistered distributor in Cook County, without regard to the fact that more than five hundred of the transactions were labeled as book transfers. *See* C 10135, 11389, 11394.

Even though the ISR alone clearly establishes that the transactions at issue are Book Out transactions, Marathon is not solely relying on the ISR. Mr. Freeman testified in detail as to how a Book Out transaction occurs and is documented by Marathon. As an example, Mr. Freeman focused on the documents created in connection with a representative matching buy/sell agreement. C 12497-12508; 10763-67. Mr. Freeman first identified and explained the terms of the original buy/sell agreement. C 12497-12508. Mr. Freeman testified that Marathon took receipt of the base gas that represents the "buy" portion of the buy/sell agreement.[2] C 12535. In contrast, the "sell" portion of the agreement was resolved via a Book Out transaction because Marathon discovered it had another independent transaction with Sunoco, in which it had agreed to buy the same

[2] The "buy" portion of the buy/sell agreement is not part of this dispute. Marathon does not have a Tax collection/remission obligation as the buyer of gas.

quantity of base gas.[3] C 12508-09, 12535. *Id*. Marathon did not enter into evidence that independent agreement with Sunoco because it is irrelevant; since Marathon was the buyer the agreement did not trigger any obligation for Marathon to collect the Tax and was not a subject of the audit.

Mr. Freeman then identified Respondent's Exhibit 9 as the physical deal sheet used internally at Marathon to document the original buy/sell agreement (of which only the sell portion is relevant). C 12530, 10792-93. Because in these agreements Marathon has the intention to both buy and receive gas, the transaction was booked as both a receipt and delivery, and two scheduling numbers – 29281 & 29282 – were assigned, reflecting the agreement to receive ("buy") and deliver ("sell") barrels of base gasoline. C 12498, 12531-34.

Mr. Freeman next identified Respondent's Exhibit 10 as the book-out letter that Marathon used internally to record the book transfer agreement. C 12537. In the book-out letter, Marathon assigned a Book Transfer Number (BT 09-12), and specifically referenced the two contracts to be offset –Sales Order No. PS 29282 (the "sell" portion of the buy/sell agreement, in which Marathon agreed to sell base gas to Sunoco), and Purchase Order No. PP 29323 (in which Sunoco agreed to sell an identical quantity of base gas to Marathon). C 10794, 12537-39. As Mr. Freeman explained, "[w]hat I'm doing is placing on one piece of paper all the transactions that are going to settle financially so we don't move anything." C 12538-39.

Mr. Freeman then identified Respondent's Exhibits 11 and 12 as the Book Transfer Invoices generated by Marathon and sent to Sunoco to reflect the book transfer

[3] The "base" gas sold did not meet the EPA standard for sale to retail consumers. C 12508-9.

(Invoice Nos. 912 and 356519, respectively). C 12540, 10795-96. These invoices contain the book transfer number (BT 09-12), the Sales Order Number assigned by Marathon to the "sell" portion of the Buy/Sell Agreement (PS 29282), and the Purchase Order Number assigned by Marathon to the Sunoco transaction (PP 20323) to be financially settled through the book transfer. C 10475-76, 12548-50.

Mr. Freeman testified that these Book Out documents, Exhibits 4 and 9 through 12, were representative of the documents Marathon used to document all its Book Out transactions. C 12550. Each of these exhibits was admitted into evidence without objection. Following Mr. Freeman's testimony, Mr. Steiner specifically tied the Book Out transaction reflected in Exhibits 4, and 9-12 to the ISR. C 12689-90. The Book Out transaction appears on page 25 of the ISR in the same line as No. 912 in the Ticket Column (reflecting Invoice 11) and No. 356519 in the Invoice Column (reflecting Invoice 12). C 8269. In the Carrier Column, the transaction is specifically identified as a book transfer. C 8269, 12689-90.

Mr. Freeman explained that although there are varying reasons why parties decide to financially terminate a contract, regardless of the reason for or type of book transfer, all are documented in the same manner. C 12484, 12488, 12492, 12494-96-31, 12550. As the circuit court and appellate court correctly concluded, the ALJ's conclusion that there was a failure to present physical evidence of each "type" of book transfer was error. A-11, A-90. The County claims in a footnote that under Illinois Rules of Evidence 1006 the ALJ had a right to require Marathon to produce evidence of every Book Out, but this ignores the ISR (which lists every Book Out at issue) and mischaracterizes the evidentiary rule, which does not contemplate a post-trial ruling that all documents related

to a voluminous record must be produced. *See* County's Br. at 29, n 10. It also ignores the fact that proceedings in administrative review before the County are not subject to the formal rules of evidence. Ord. Sec. 34-81(c).

As demonstrated above, the County's argument that Marathon offered no documentary evidence of the Book Outs is plainly erroneous. *See* County's Br. at 22-31. Marathon introduced ample books and records to support the testimony of its witnesses. The County argues a "contract supporting the terms of the supposed book transfer" is missing, but there is no missing Book Out contract. *See* County's Br. at 22-23, 28. The County simply misunderstands the testimony and inserts confusion where there is none. Marathon witnesses identified and explained all the books and records Marathon relies upon to document an agreement to Book Out a transaction. As reflected in the book-out letter (Respondent's Exhibit 10) and the invoices (Respondent's Exhibits 11 and 12) that were introduced into evidence, a Book Out is achieved by a financial settlement, with no change in possession or ownership of gas. C 10794-96. Moreover, the two contracts that are subject to the Book Out are specifically referenced in the book-out letter (Respondent's Exhibit 10) and the invoices (Respondent's Exhibits 11 and 12), and the Book Outs appear on the ISR. C 8244-8304, 10794-96. There is no separate document that exists that contains the contractual terms of the Book Out transaction. The County's assertion that Mr. Freeman testified there was a written Book Out contract is erroneous. *See* County's Br. at 22. Instead, Mr. Freeman testified repeatedly that Marathon's schedulers talk with their exchange partners to determine which contracts should be financially booked out and documented their agreement via Respondent's Exhibits 10-12. C 12536-38, 12545, 12550-51, 12559-60. Also contrary to the County's allegation, just

as in *County of Cook v. BP Products North America, Inc.*, No. RD-16011 & RG-16010 (Jan. 31, 2022), the Marathon buy/sell agreement expressly contemplated that the transaction could be resolved by Book Out. *See* County's Br. at 31-32; C 10764 (Payment Terms, stating: "If delivery takes place by book transfer, payment is due on the effective date of the book.").

The County's effort to characterize Marathon's documentary evidence of Book Out transactions as "vague," "nondescript sheets" of information and "circumstantial evidence" also fails. *See* County's Br. at 25, 31-32. The County now admits that Marathon was not required to provide "conclusive" evidence, but rather simply documentary evidence of the Book Out transactions. County's Br. at 31. The documents of record plainly meet this standard. The County also mischaracterizes the testimony of Marathon's witnesses, failing to mention their experience, their familiarity with Marathon's processes and their detailed explanation of the Marathon books and records that were admitted into evidence. *See* County's Br. at 29. Contrary to the County's assertion, this was not an instance where only oral testimony was presented, as a substitute for missing books and records. *See* County's Br. at 25-26. Mr. Freeman and Mr. Steiner's testimony – explaining the meaning of Marathon's own records, of which they had personal knowledge – is relevant and must be considered. *See, e.g., Feldstein v. Dep't. of Fin.*, 377 Ill. 396, 399 (1941), (holding that a taxpayer' books and records, together with the testimony of its witnesses regarding those books and records, was sufficient evidence to overcome the Department's prima facie case); *Miller v. Dep't. of Revenue,* 408 Ill. 574, 581 (1951) (distinguishing *DuPage Liquor Store v. McKibbin,* 383 Ill. 276 (1943) and holding that the testimonial and documentary evidence present by the

taxpayer was sufficient to overcome the prima facie case made by the Department's corrected return). There was no suggestion at the hearing or in the ALJ's ruling that Marathon's witnesses were not qualified to explain the meaning of the documents admitted into evidence.[4] The County also fails to mention that its motion to strike Freeman's testimony at the hearing, for reasons like those expressed in its brief to this Court, was denied.[5] C 10668.

### B. Illinois case authority supports the conclusion that Marathon met its burden of proof

Marathon met its burden of proof by relying upon the ISR, a compilation document, the documents related to the Sunoco book transfer, and the testimony of its witnesses. Marathon was not required to produce every single deal sheet, book transfer letter, and invoice to support its testimony that the book transfers on the ISR were payments in which no Motor Fuel was transferred. Illinois case authority establishes that when a fact may be ascertained only by the inspection of a large number of documents comprised of detailed statement (more than 500 book transfers are listed on the ISR), a summary of those documents may be received into evidence. *In Re Marriage of Delarco,* 313 Ill.App.3d 107, 115-6 (2nd Dist. 2000); *see also F.L. Waltz, Inc. v Hobart Corp.* 224 Ill.App.3d 727, 731 (3d Dist. 1992). Compilation documents, which aggregate and assimilate information from numerous other documents, are admissible, probative

[4] As discussed in Section I.C., the County did not rebut this testimony in any manner.

[5] During the administrative hearing there was a detailed exchange between Mr. Freeman and the ALJ regarding the book transfer process. C 12486-91. The ALJ did not state that she did not understand the facts presented, or that there had been any deficiency by Marathon in its presentation of evidence. To the contrary, the ALJ repeatedly asked the County to confirm its understanding of the *legal* issue presented. C 3824-44. The ALJ's ruling, finding a failure of proof, coming nearly two years after the hearing, was a surprise.

evidence. *Id.* This is particularly true here, where the County relied upon the same ISR in support of the Revised Tax Assessments and offered no evidence disputing the Sunoco book transfer documents and related testimony. It was clear error for the ALJ to ignore the testimony of Marathon's witnesses and representative supporting records, which were unrebutted. *See, e.g., Goldfarb v. Dep't. of Revenue,* 411 Ill. 573, 580-81 (1952) (overturning tax assessment after finding the lower court rejected the competent testimony of the taxpayer and ignored the sufficiency of the taxpayer's records), stating:

> The positive testimony of the taxpayer has not been refuted or impeached, in spite of the fact that the auditors had possession of all his books and records and ample opportunity to determine and show if they were incorrect or false in any respect. Under these circumstances, the court will not assume the taxpayer testified falsely. … the trial court erred in affirming the final assessment …

*See also Novicki v. Dep't. of Fin.,* 373 Ill. 342, 346 (1940) (finding that the taxpayer provided "positive testimony that his books were true and correct," and holding that "with the [taxpayer's] evidence uncontradicted, the prima facie case made by the proposed assessment was overcome, the burden shifted to the [state] to prove its case by competent evidence. This it failed to do.")

### C. The County failed to rebut Marathon's evidence

The County asked this Court to reject Marathon's testimony regarding the meaning of its records in favor of generic definitions and an unrelated third-party glossary of terms, borrowed from another context. The ALJ did not rule on these issues, but even if it had, it would be subject to reversal. A finder of fact may not simply reject unrebutted testimony, and it may not discount witness testimony unless it was impeached, contradicted by positive testimony or by circumstances, or found to be inherently

improbable. *Sweilem v. Illinois Dept of Revenue*, 372 Ill.App.3d 475, 485 (1st Dist. 2007).

As the County must admit, it introduced no evidence of contrary facts nor evidence of inherent improbability at the hearing of this matter. In fact, the County presented not a single piece of evidence to contradict Marathon's books and records and corroborating testimony. In its case in chief, the County's auditor admitted that he failed to consider that the transactions the County sought to tax were book transfers. C 10135 ("I didn't pay too much attention to what a book transfer was or wasn't.") The County's auditor concluded there was a sale subject to the Motor Fuel Tax simply because money changed hands. C 10156 ("So if you tell me that you sold me something for a price, that's a sale.") In contrast, Mr. Steiner gave a detailed explanation of how Marathon recorded its Book Out transactions in the accounting system which are shown on the ISR. He explained that because the ISR does not have specific columns related to book transfers, Marathon recorded the book transfers in the fields existing in the system, placing "book transfer" as an entry in the Carrier column, and stating "Chicago" to reference the Chicago pricing region in the Origin and Destination columns. C 12682-84. The County presented no evidence to the contrary. As the ALJ pointed out:

> All of Marathon's witnesses…were available for cross-examination and cross examination did in fact occur….Not only cross-examination, but there was a hearing opportunity that could have been taken for the Department of Revenue to say…we want to bring in rebuttal witnesses to – to Mr. Freeman and Mr. Steiner …on the issue of book-outs as Mr. Freeman and Mr. Steiner understand it from the point of view of being employees of Marathon…the Department could have asked for an opportunity to present other witnesses on their side that would rebut Mr. Freeman's and Mr. Steiner's testimony. And that did not occur.

C 3881-82. As a result, there is nothing in the record to support the County's naked assertion that Marathon's ISR entries falsely report the existence of Book Out transactions.

For all of these reasons, the central premise of the County's brief fails.

## II. The County's Arguments that the Ordinance Taxes the Book Out Transactions Are Contrary to the Evidence and the Plain Language of the Ordinance.

### A. The County's argument that Motor Fuel Tax is due in the absence of a retail sale ignores the plain language of the Ordinance

Buried in the middle of the County's brief is its response to the crux of this case, which is that the Motor Fuel Tax is only imposed on the physical transfer of possession or ownership of Motor Fuel for retail sale. *See* County's Br. at 38-39. The Book Out transactions are not subject to the Motor Fuel Tax under the plain and unambiguous text of the Ordinance because there was no transfer of Motor Fuel for retail sale. The County's argument that Marathon had an obligation to collect and remit tax on transactions that ultimately do not result in retail sales of Motor Fuel is wholly without merit.

The County erroneously asserts that Marathon's collection obligation is not only triggered by a "retail sale," rather it is triggered any time a distributor "sells" fuel. *See* County's Br. at 36. The County fundamentally misunderstands its own Ordinance. The County's interpretation of the Ordinance ignores the plain language of Section 74-472(c), which requires "collection of *the tax levied in this Article* upon the sale of gasoline…" Ord. Sec. 74-472(c) (emphasis added). The tax is "levied" under Section 74-472(a), which provides that the "tax is hereby imposed on the *retail sale* in Cook County of gasoline, diesel fuel..." Ord. Sec. 74-472(a) (emphasis added). Thus, under the plain

language of the Ordinance, Marathon was only required to collect the tax if there would ultimately be a retail sale of fuel. In a Book Out, a transaction is financially settled, with no exchange of Motor Fuel. As a result, there can be no retail sale, and the Motor Fuel Tax does not apply.

The County's argument also ignores the second sentence of the definition of "sale" which provides that "[i]n every case where gasoline, diesel fuel, biodiesel, or gdiesal fuel are exchanged, given or otherwise disposed of, it shall be deemed to have been sold." *See* Ord. Sec. 74-471. The Ordinance's inclusion of the phrase "disposed of" relates to the "disposal" of actual, physical product – Motor Fuel. To conclude otherwise would enlarge the scope of the Tax beyond the intent of the drafters, which was to tax the retail sale of Motor Fuel in Cook County. This precise rationale was employed by the same ALJ to conclude in the companion *BP Products* case that "[t]he plain language and clear intent of the Ordinance is to tax only transactions involving the sale of gasoline and diesel fuel specifically at the retail level, not to tax monetary payments that settle contracts to sell or purchase gasoline or diesel fuel because no gasoline or diesel fuel can ever be sold at the retail level when contracts are settled monetarily." A-145, A-157.

The plain language of the Ordinance does not extend to tax the Book Out transactions at issue. To the extent this Court finds there is any ambiguity in the scope of the Tax, any such ambiguity must be construed strictly in favor of Marathon and against the County under well-established case law. *See* Marathon's Br. at 19-20.

The County misstates Marathon's argument that applying the Motor Fuel Tax to transfers of *intangible property* reads the retail sales sale requirement out of the Ordinance, by erroneously asserting that Marathon argued that the Tax did not apply to

transfers of *ownership* of property. *See* County's Br. at p. 41-42. The entire ensuing section of the County's brief labors under that misstatement, even arguing that the anticipated transfer of ownership or possession should be sufficient to impose the tax, as it creates a "rebuttable presumption" that taxation is appropriate. *See* County's Br. at 42-43. The County never offers any explanation, however, for Marathon's real argument – that the plain intent of the Ordinance is to tax transactions involving only the sale of Motor Fuel, not to tax monetary payments that settle contracts to make such sales. Despite admitting that distributors have the right to rebut an assessment by demonstrating, via their books and records, that Motor Fuel was never ultimately sold, the County refuses to acknowledge, must less understand, Marathon has done just that. *See* County's Br. at 43.

### B. The County's arguments that there was transfer of ownership such that there was a "sale" under the Ordinance misstate the facts and the law

Even if this Court determines that a retail sale is not required for the imposition of the Motor Fuel Tax, there is nothing in the record to support a conclusion that there was a "transfer of ownership or possession" such that a Book Out transaction constitutes a taxable "sale" under the Ordinance. The County doesn't contend that there was any transfer of possession of Motor Fuel so the only question before this Court is whether there was a transfer of ownership. Despite the County's arguments to the contrary, none of the documentary evidence even suggests a transfer of ownership occurred. Moreover, Marathon's witnesses testified definitively that the Book Out transactions did not entail a transfer of ownership. C 12467, 12490, 12497, 12690. Notably the County did not cross examine any of the Marathon witnesses on this point. Nor did it impeach or otherwise

call into question the consistent, credible testimony of Marathon's witnesses to the effect that the Book Out transactions did not result in transfers of ownership of gasoline or fuel. C 3881-82. The County's resort to external definitions of Book Out transactions is insufficient to overcome the direct testimony of Marathon's witnesses who defined what the term meant to Marathon.

Despite this uncontroverted evidence, the County strains to argue that Marathon engaged in a taxable transaction because there was a transfer of ownership that triggered a "sale" within the meaning of the Ordinance. *See* County's Br. at 32-45. All of its arguments fail for the reasons described below.

**1. The Book-Outs did not involve a "present" transfer of ownership**

The County first argues that by its reference to matching buy/sell agreements in its opening brief as "forward" contracts, Marathon admitted that the Book Outs were agreements by which a commodity "is *presently* sold but its delivery is, by agreement, delayed or deferred," thus evidencing a change in ownership. County's Br. at 34. Of course, Marathon said nothing of the sort in its brief. It simply used the phrase "forward contract," and it specifically referred to Book Out transactions as "financial settlements of forward contracts." *See, e.g.,* Marathon's Br. at 8, 18. This is consistent with the testimony of its lay and expert witnesses, who identified the Book Outs as forward contracts that were settled financially, with no change in ownership or possession. *See, e.g.*, the testimony of Mr. Freeman (neither title to, nor possession of, Motor Fuel changes from one party to another in a Book Out transaction) (C 12475-76, 12551-52), Mr. Steiner (corroborating Freeman's testimony and confirming that Motor Fuel and inventory levels never change in the Book Out transactions (C 12681, 12690-91), and Dr.

Arburn (testifying that "My understanding of a book-out transaction is essentially a forward contract, a transaction that two parties have agreed to financially settle.") (C 12412-13). Later, when asked whether the settlement of a forward contract was similar to a Book Out transaction, Dr. Arburn agreed that was true, then testified a "Book-out is to financially settle it whereas in a forward contract you publicly would deliver. But a book-out is just a financial way to settle the contract." C 12416. The County falsely asserts that Dr. Arburn admitted that book transfers involve the transfer of ownership of fuel, when in fact he made no such statement. *See* County's Br. at 46 (citing C 5023).[6]

Contrary to the County's assertion, the argument that Marathon's Book Out transactions were "present" sales, where ownership of motor fuel was transferred as of the date of the contract, is not supported by the language of the buy/sell agreement. C 10763-67. The agreement does not provide that ownership of the motor fuel is transferred as of the date the contract was executed. Key terms of the agreement, including the Payment Terms and Taxes sections, refute the County's contention because they do not take effect until there is either a purchase and delivery of product, or a Book Out. C 10764. The Payment Terms section states that payment is not due until after delivery of "relevant pipeline meter ticket or supporting documents" reflecting transfer of

[6] The County criticizes Dr. Arburn for not testifying about the documents of record, but he was not a fact witness. *See* County's Br. at 7, 27. Rather, the purpose of his testimony was to assist the ALJ in its understanding of the subject matter by clarifying complex concepts, and explaining a difficult topic of which he has superior knowledge. There is no evidentiary failure associated with his testimony. The County's repeated reference to Marathon's alleged violation of the best evidence rule is also inappropriate in this setting because the County's administrative hearings are not subject to the Illinois Rules of Evidence. Ord. Sec. 34-81(c) ("The hearing officer is not bound by the technical rules of evidence.") *See* County's Br. at 25, 27.

motor fuel or a "book transfer." *Id.* Similarly, the Taxes section states that the buyer does not become responsible for any taxes related to the transaction until after the product is "purchased and delivered to it by the Seller." *Id.*

Nor does the legal authority cited by the County support the County's argument, even in the bankruptcy context. The County argues that the fact that the buy/sell agreement provides that the parties are "Forward Trading Merchants" under Section 101(26) of the Bankruptcy Code incorporates a "present" sale requirement.[7] See C 10756. However, that section of the Bankruptcy Code neither defines a forward contract nor incorporates the concept of a "present" sale. Rather, it defines a "forward trading merchant" as "a Federal reserve bank, or an entity the business of which consists in whole or in part of entering into forward contracts as or with merchants in a commodity (as defined in section 761) or any similar good, article, service, right, or interest which *is presently or in the future becomes the subject of dealing in the forward contract trade."* 11 U.S.C. § 101(26) (emphasis added). Subpart 25 of Section 101 defines a "forward contract," again without reference to the requirement of a "present" or immediate transfer of ownership, as "a contract …. For the purchase, sale, or transfer of a commodity, as defined in section 761(8) of this title, or any similar good, article, service, right, or interest *which is presently or in the future* becomes the subject of dealing in the forward contract trade, …" 11 U.S.C. §101(25)(A) (emphasis added). The remaining language in the Subsection definition of "forward contract" similarly does not incorporate any requirement of a "present" sale.

[7] There is no support in the record for the County's assertion that the buy/sell agreement contains a typographical error. *See* County's Br. at 5, n.2.

The cases cited by the County also do not support the conclusion that a "present" sale is a required element of a forward contract. *See* County's Br. at 34. To the extent they refer to a "present" transfer, the cases examine whether a sale of grain is a "cash forward transaction" or a futures contract subject to regulation by the Commodities Exchange Act. *See CFTC v. Zelener,* 387 F.3d 624, 626, n.2 (7th Cir. 2004) ("A 'cash forward' transaction, in contrast, refers to a transaction in which the commodity is presently sold but its delivery is, by agreement, delayed or deferred."); *see also Grain Land Coop v. Kar Kim Farms,* 199 F.3d 983, 991 n.2 (8th Cir. 1999); and *Salomon Forex, Inc. v. Tauber,* 8 F.3d 966, 970 (4th Cir. 1993).[8] The authority cited by the County in its footnote 14 in support of its argument that the term "cash forward transaction" is used interchangeably with "forward contract" does not support this conclusion. *See* County's Br. at 34. The cited cases emphasize that the key feature of a forward contract is not an immediate transfer of ownership (in fact, that is not mentioned), but rather the expectation that delivery will occur in the future. *See, e.g., In re Olympic Natural Gas Co.,* 294 F.3d 737, 741 (5th Cir. 2002):

> Furthermore, our interpretation is in accord with the traditional definition of "forward contract." Although the trustee points to the fact that the transactions at issue here contemplated actual delivery as evidence that they are not true "forward contracts," courts in other circuit have repeatedly stated that one of the distinguishing characteristics of a forward contract is that the parties expect to make actual delivery.

*See also Dzurka Bros., LLC v. Luckey Farmers, Inc.,* No. 1:23-CV-11038, 2024 WL 268140 at *6 (E.D. Mich. Jan. 24, 2024) ("In contrast to the fungible quality of futures, … forwards [contracts] are generally individually negotiated sales of commodities

[8] The language is found nowhere in the first case cited by the County, *Andersons, Inc. v. Horton Farms, Inc.,* 166 F.3d 308, 318 (6th Cir. 1998).

between principals in which actual delivery of the commodity is anticipated, but is deferred for reasons of commercial convenience or necessity.")

Finally, the County's effort to distinguish forward contracts from futures contracts, regulated by the Securities and Exchange Commission, are unavailing and frankly, irrelevant. The County asserts in a footnote that because forward contracts are not subject to regulation, the ruling in this case will not "affect the trade in futures on exchanges." County's Br. at 43, n. 15. Unfortunately, the County misses the mark again. What the County asserts here, and what the appellate court has erroneously concluded, is that the Motor Fuel Tax can be applied to sales of intangible interests. Both forward and futures contracts involve such sales. The application of a tax meant for the sale of tangible personal property, like the Motor Fuel Tax, to the sale of an intangible right creates serious risk for all sales of intangible interests, regardless of whether they are subject to SEC regulation.

**2. The designation "F.O.B. Chicago" does not imply an immediate transfer of ownership**

The County then argues that even absent any language in the contract making clear that the matching buy/sell agreement was a forward contract "effecting an immediate transfer of ownership of fuel," there still would have been a transfer of ownership because the agreement included the language "F.O.B. Chicago, IL." County's Br. at 35. Citing a 2003 Pennsylvania state court decision, the County argues that "Free on Board" is a "legal term used to indicate that formal title to a good will transfer to the purchase upon its arrival in the geographic location specified." *Id.* According to the County, this provision reflected a conditional agreement of sale, and therefore triggered the imposition of Tax.

This argument is a nonstarter because it uses an inaccurate definition of "free on board." This Court defines "free on board" not as when title passes, but as a provision indicating which party is to bear the expense of shipment. *See, e.g., Harman v. Washington Fuel Co.* 228 Ill. 298, 81 N.E.1017, 1019 (1907) (stating that "free on board" means "that the goods are to be furnished by the seller on board free of all charges and expenses up to and including" the point of delivery."). *See also Bruel and Kjaer v. Vill. of Bensenville,* 2012 IL App (2d) 110500 (2012) at ¶ 19 ("F.O.B. is an abbreviation for 'free on board,' a term used in transactions in tangible goods, and is defined in the UCC.")

**3. The Book Outs were not a "conditional" sale**

The reference to "F.O.B. Chicago" does not prove the existence of a taxable "conditional" sale because the condition – delivery of fuel to Chicago for retail sale – was never satisfied. Instead, the Ordinance's reference to a "conditional" transfer of ownership as a "sale" applies to transactions where the condition is triggered. Here, no Tax is due because the contract was resolved via financial settlement, with no transfer of ownership or possession of Motor Fuel. Had the condition been satisfied – meaning delivery of the Motor Fuel as originally contemplated by the buy/out agreement – a Tax obligation would have been triggered. This is consistent with any sale of a tangible good – if the sale does not take place, tax on the sale price is not owed.

Moreover, the County's characterization of the buy/sell agreement as a "conditional" sale is contrary to the commonly understood meaning of the phrase. *See* County's Br. at 35. The Ordinance does not define what is meant by a "conditional" sale. There are two commonly understood meanings, neither of which is applicable here. In

the first, a "conditional sale" is a sales contract in which the buyer takes possession of an asset, but the title remains with the seller and the seller maintains the right to repossession until the purchase price is paid in full. *See, e.g., Conner v. Borland-Grannis Co.,* 294 Ill. 58, 128 N.E. 317, 318 (1920); *Ford Motor Co. v. Nat'l Bond & Investment Co.,* 294 Ill. App. 585, 14 N.E.2d 306, 310 (1st Dist. 1938). This type of sale is commonly used for the purchase of higher priced items like homes, vehicles, and aircraft. In Illinois, the phrase "conditional sale" is also used by the Illinois Department of Revenue ("Department") to describe a type of lease in which possession of the leased property is delivered to the lessee at the termination of the lease after a nominal – for example, $1.00 – payment. By regulation, the Department views such transactions as sales, rather than leases, subject to tax upfront on the entire purchase price. *See, e.g.*, 86 Ill. Admin. Code 130.2010(a), ST-22-0006 (04/12/2022), ST-0016-GIL (03/16/2015) and Chapter 16.1 of the Department's Sales Tax Audit Manual. The buy/sell agreement meets neither of these commonly understood meanings and cannot be considered a "conditional" sale under the Ordinance.

**4. The County misconstrues Marathon's citation of case authority defining "ownership"**

Despite the County's argument to the contrary, by citing to Illinois authorities Marathon is not asserting that a sale only occurs when there is a "transfer of control and possession or possession or both." *See* County's Br. at 37. Rather, the case law cited supports the conclusion that in order for there to be transfer of ownership there must be a transfer of control *or* possession of the Motor Fuel. *See* Marathon's Br. at 22-23; *People v. Chicago Title & Trust Co.*, 75 Ill.2d 479, 489 (1979) ("The key elements of ownership are control and the right to enjoy the benefits of the property.") It is appropriate to

consider the Illinois common law definition of "ownership" because the term is not defined in the Ordinance.

There is no dispute between the parties that there was no transfer of possession. Nor does the evidence support the conclusion there was a transfer of control. Here, the contracting parties never acquired a right to control or use the Motor Fuel. Thus, there was no transfer of ownership of the Motor Fuel and no "sale" subject to the Motor Fuel Tax.

**5. The County misconstrues Marathon's reference to other provisions in the Ordinance**

Contrary to the County's argument, Marathon did not cite Sections 74-472I and 74-472(f) of the Ordinance out of context. *See* County's Br. at 39-41. Both provisions support the conclusion that under the Ordinance, possession of motor fuel (not the settlement of an intangible interest) is required for taxation to be imposed. Section 74-472(c) contains prefatory language, quoted by Marathon, that distributors or retail dealers *in possession of* Motor Fuel on the date of the enactment of the Ordinance may be subject to special rules requiring tax collection. Similarly, Section 74-472(f) of the Ordinance provides that retail dealers *receiving* Motor Fuel need not pay tax until thirty days after *receipt.* Incredibly, while continuing to maintain that Marathon remains subject to tax despite the financial settlement of its Book Outs, with no transfer of ownership or possession, the County touts the thirty-day after receipt payment provision in Section 74-472(f) as making "eminent practical sense" in order to avoid "inadvertent over-remittance by retailers," who might not actually receive *possession* of the Motor Fuel in question or might pay tax on Motor Fuel for which a distributor has already collected and remitted tax. *See* County's Br. at 41.

The County attempts to circumvent the arguments in Marathon's brief about sales to unregistered distributors by arguing that dealers who engage in Book Outs with Marathon may have been required to register as distributors because of other activities unrelated to the Book-Outs. *See* Marathon's Br. at 17-19; County's Br. at 43-45. This misses the point. Marathon's argument was that the County is contending that Motor Fuel Tax is due under Sec. 74-472(c)(3) of the Ordinance, which requires tax collection from "[a]nother Gas Distributor doing business in the County that is not holding a valid registration certificate," even though the County's auditor admitted that the parties engaging in Book Outs had not participated in any activity in the County that would trigger a duty to register under Ordinance Sec. 74-474. C 10141-45. Since tax collection is only due from an unregistered distributor doing business in the County (therefore by definition required to register), the County's argument that Book Outs are subject to tax is inconsistent with the registration requirement.

### C. The County's argument that "direct" Book Outs are subject to tax fails

The County argues that even if Marathon proved the existence of Book Outs, its "direct" book out transactions are subject to the Motor Fuel Tax. County's Br. at 45-49. This argument fails for a number of reasons. First, it rests on the mistaken assertion that Marathon documented its Book Out transactions in different ways. As demonstrated above, Marathon used the same procedure to document all Book Outs. Second, it erroneously asserts that Marathon's expert Dr. Arburn testified that Book Outs "can involve the transfer of ownership of fuel." *See* County's Br. at 46. To the contrary, Dr. Arburn testified that Book Outs may involve the sale of intangible interests in a commodity, resolved via financial settlement so that product is not transferred. C 12417.

Third, the County asserts, without record or legal support, that "direct" Book Outs create a "contractual ownership right" that must be transferred even if financially settled. County's Br. at 47-48. The County goes on to argue, without support, that somehow the seller could sue for anticipatory breach of contract if it learned that the purchaser intended to dispose of that fuel. *Id*. This assertion is contrary to the plain language of the buy/sell agreement, which creates no immediate transfer of an ownership interest, and specifically contemplates that the agreement may be resolved by Book Out.

The County also misconstrues Mr. Freeman's testimony regarding the right of cancellation. What Freeman testified to is that the contractual obligations to transfer ownership and possession of Motor Fuel under the original agreements cannot be cancelled and if they cannot be fulfilled then they must be settled with some monetary exchange or financial settlement. C 12471-76. The buy/sell agreement provides that delivery can take place by book transfer. C 10764. Thus, the contract is fulfilled by virtue of the Book Out (a financial settlement) and not by transfer of ownership or possession of Motor Fuel (a physical settlement) and no transfer of ownership occurs.[9]

Finally, contrary to the County's assertion, *Dep't. of Transportation v. Anderson,* 384 Ill. App. 3d 309 (3rd Dist. 2008) does not support the County's assertion that a "transfer of ownership of fuel is necessary for a direct book transfer to have its desired effect, …" *See* County's Br. at 47. The *Anderson* decision discusses the transfer of ownership of a real estate parcel; it does not address the subject of Book Outs. *Anderson* reiterates the common law meaning of "ownership" that is referenced in the cases cited

[9] Marathon's witnesses also testified that in Book Out transactions there is no meter ticket that shows physical movement of the product nor transfer order that tells the terminal to move product. C 12466-67, 12551, 12690.

by Marathon in its opening brief. *Id.* at 312 ("The primary elements of ownership are the rights of possession, use and enjoyment, …"). Clearly, the "desired effect" sought by the County is taxability, but neither the facts of record nor legal authority support this conclusion for any of Marathon's Book Out transactions.

## III. The County Failed to Meet its Burden of Proof.

The County falsely asserts that unlike any other state taxing authority, including the State of Illinois, it had no duty to use its best judgment and information in issuing Marathon's tax assessment. *See* County's Br. at 19-21. The suggestion that an Illinois taxing authority has no duty to act reasonably is ludicrous. As a home rule authority, the County's power to tax is derived from the Illinois Constitution, which imposes a duty of reasonableness on all taxing authorities. Article IX, Section 2 of the Illinois Constitution states:

> In any law classifying the subjects or objects of non-property taxes or fees, the classes *shall be reasonable* and the subjects and objects within each class shall be taxed uniformly. Exemption, deductions, credits, refunds and other allowances *shall be reasonable*.

Ill. Const., Art. IX, Sec. 2 (emphasis added). The County's argument is also directly contrary to its own Ordinance, which recognizes in several contexts the requirement that it must use its best judgment in taxing matters. For example, the Ordinance requires the County to use its "best judgment and information" in issuing a penalty award. Ord. Sec. 34-83(a). Similarly, in the case of a jeopardy assessment, where a taxpayer has failed to respond to an audit notice, the Ordinance provides that the County must issue a tax determination and assessment "based on the best estimate of the person's tax liability." Ord. Sec. 34-63(c)(2)(a). Obviously, the County cannot be relieved of an obligation to act with reason when it issues a tax assessment to a taxpayer like Marathon that has

dutifully responded to an audit notice, but then be required to act with reason when issuing an assessment to a taxpayer that has ignored an audit notice. Rather, per the Illinois Constitution, the duty of reasonableness extends to all the County's tax assessments.

Given the Illinois Constitution's requirement that the County act reasonably, the authority cited by Marathon in support of its argument that the County failed to establish its prima facie case in its opening brief is relevant and controlling. *See* Marathon's Br. at 31-34. Rather than address Marathon's arguments head on, the County resorts to claiming that Marathon forfeited the argument. The County falsely asserts that Marathon failed to raise this argument before the ALJ when in fact Marathon's counsel raised the issue with the ALJ. *See, e.g.*, C 3820 ("And so it also supports, I think, that this is a flawed audit, and that they really haven't met their burden to say that it was prima facie correct.") Marathon raised the argument again at the circuit court level and before the appellate court. Clearly, the argument was not forfeited.

Moreover, forfeiture is a limitation on the parties, not on the court, which has discretion to decline to apply forfeiture "where necessary to obtain a just result or maintain a sound body of precedent." *Walworth Invs.-LG, LLC v. Mu Sigma, Inc.,* 2022 IL 127177, ¶ 94, 215 N.E.3d 843, 869, *reh'g denied* (Jan. 23, 2023). *See also Our Savior Evangelical Lutheran Church v. Saville,* 397 Ill. App. 3d 1003, 1028, 922 N.E.2d 1143, 1163 (2d Dist. 2009) (*Id.)* and *In re H.B.,* 2022 IL App (2d) 210404, ¶ 43, 220 N.E.3d 361, 373 ("Forfeiture is a rule of administrative convenience and does not preclude us from considering an otherwise forfeited contention. Indeed, forfeiture is a limitation on the parties, not this court.").

Whether viewed as a prima facie case obligation, or as rebuttal evidence, the record is clear that the County failed to meet its burden of proof.

## IV. The County's Interpretation of the Ordinance Results in Constitutional Infirmities.

### A. The County's arguments that taxation of the Book Out transactions does not result in an unconstitutional occupation tax are unavailing

The County erroneously alleges that Marathon has forfeited its argument that the imposition of the Motor Fuel Tax on the Book Out transactions results in an unconstitutional occupation tax. *See* County's Br. at 50. The County is apparently claiming forfeiture because Marathon did not explain to its satisfaction how the application of the Tax on the Book Out transactions imposes a tax on the privilege of engaging in the occupation of a distributor. *Id.* There was no forfeiture because Marathon argued in its opening brief that the Motor Fuel Tax is only imposed on the transfer of tangible personal property and if the Tax is imposed on Book Out transactions the legal incidence of the Tax falls on Marathon, which results in an unconstitutional occupation tax. *See* Marathon's Br. at 13-19. 27-29. These arguments were sufficient because this Court has applied the "legal incidence" test to determine whether a tax is an occupation tax when the tax is on sales of tangible personal property. *See, e.g., Commercial Nat'l Bank v. City of Chicago*, 89 Ill. 2d 45, 63-64 (1982).

In response to Marathon's arguments, the County erroneously contends that somehow "the ultimate legal responsibility for the Tax would still ultimately lie on the consumers who pay that tax at the time of purchase at retail, thus reimbursing the person from whom the consumer purchased that fuel for any amounts previously collected" when in actuality the Book Out transactions do not result in any transfer of Motor Fuel

that could ultimately be sold to a consumer. *See* County's Br. at 51. The County also erroneously alleges that Marathon merely "speculates" that the Book Out transactions "might not result in a retail sale to a consumer in the County." *Id.* Nowhere in its brief does Marathon speculate that the Book Out transactions might not result in a retail sale. Instead, Marathon asserts, with certainty, that the Book Out transactions did not result in a retail sale. *See* Marathon's Br. at 14-15, 28-29. As the uncontroverted evidence established, the Book Out transactions were purely financial transactions that involved no transfer or exchange of Motor Fuel. If no Motor Fuel was transfer or exchanged, there is no doubt that there was no Motor Fuel for a party to sell to a consumer in a retail sale. Thus, the Motor Fuel Tax as applied to Marathon's Book Out transactions is an illegal occupation tax because the legal incidence of the Tax falls on Marathon.

Even if this Court rejects Marathon's contention that the Motor Fuel Tax is only imposed on the retail sale of tangible property (Motor Fuel) and instead finds that it is imposed on transfers of intangible property (as the County asserts in this brief and the appellate court held), the result is still an unconstitutional occupation tax. This Court has interpreted the constitutional prohibition against taxes on occupations to include taxes on services. *Commercial National*, 89 Ill.2d at 77-80. This Court has also explained that an impermissible tax on services is broadly defined to include taxes on all "sales of transactions other than sales of tangible property," thus including the sale of intangibles. *Waukegan Cmty Unit School District No. 60 v. City of Waukegan*, 95 Ill. 2d 244, 254 (1983). When a tax is imposed on the sales of services, including sales of intangibles, then this Court will employ a "practical operations" test. *Commercial National*, 89 Ill. 2d at 65-66; *Waukegan*, 95 Ill. 2d at 255. Under a practical operations test, a tax is an

unconstitutional occupation tax if it places all of the responsibility for the tax on the person engaged in the business of providing the services. *Waukegan*, 95 Ill. 2d at 255. Here, the practical operation of the Motor Fuel Tax is plainly on Marathon because Marathon is required to pay the Tax. Moreover, the Ordinance makes Marathon liable for any Tax not collected from or paid by a retail buyer, imposes record-keeping obligations on Marathon, and imposes penalties on Marathon for non-collection and non-payment of the Tax. Ord. Sec. 74-472, 74-478. Thus, the Motor Fuel Tax as applied to Marathon's Book Out transactions is an unconstitutional occupation tax.

### B. The County's arguments that taxation of the Book Out transactions does not result in an unconstitutional extraterritorial tax are unavailing

The County attempts to refute Marathon's argument that the Tax is unconstitutionally extraterritorial by claiming a failure of proof; insisting that the buy/sell agreement's reference to "F.O.B. Chicago" must be construed to mean a Chicago delivery location. *See* County's Br. at 53-55. The County's argument is belied by Mr. Freeman's detailed testimony regarding the meaning of the buy/sell agreement, including that the references to Chicago were references to a pricing region, not to a point of delivery. Mr. Freeman prefaced this testimony by stating that it was "very, very important" because it would "strike at the heart of what we just mentioned about what does 'Chicago' mean." C 12515. He then testified in detail regarding, among other matters, what was meant by the agreement's reference to "generic Chicago pipeline." C 12515-17. Mr. Freeman went on to explain that the agreement's references to "Chicago" were references to the Chicago pricing region, and he explained that oil price information

services used in the industry set the contract price based on the region identified in the agreement, using the average price for the region on the agreement's date. C12517-25.

As it does throughout its brief, the County argues the court must ignore Mr. Freeman's testimony. The County's argument overlooks that Mr. Freeman was testifying about Marathon's own books and records: documents with which he was intimately familiar. The County is correct that a taxpayer must produce books and records in support of its tax position, but Marathon has done that. Marathon was entitled to present witness testimony explaining its books and records and there is no legal basis upon which to discount that testimony. The County also erroneously asserts that Marathon is reading terms out of the buy/sell agreement. To the contrary, Mr. Freeman explained how the company used the terms referenced in the agreement.[10] As the ALJ clarified with Mr. Freeman during his testimony: "So your testimony is FOB Chicago, Illinois, means FOB Chicago pricing region?" To which Mr. Freeman responded "Yes, Ma'am. Exactly." C 12526.

The County's arguments on extraterritoriality should also be rejected because they are directly contrary to statements made by its counsel made during the administrative hearing. During Mr. Freeman's testimony explaining the buy/sell agreement, counsel for the County objected on relevance grounds. In response to the objection, Marathon's counsel explained that the testimony was offered "[b]ecause the County has made the

[10] A review of the citation offered by the County in support of its assertion that Mr. Freeman "admitted" the Chicago FOB Chicago reference did not mean anything reflects that the statement is taken out of context. *See* County's Br. at 54; C 12521. After describing at length that references to "Chicago" were references to a pricing region, Mr. Freeman stated: "So that's what Chicago is all about. Because right after that it says FOB Chicago, Illinois. That doesn't mean anything. It just means it's the Chicago region. It's not the physical delivery location. It's a pricing reference." C 12521. There is no evidence to the contrary.

position that these all say FOB Chicago and that it's being delivered into the City of Chicago." C 12512. In response, counsel for the County stated, "The County made no claim that it was being delivered into the City of Chicago." *Id.* Counsel for Marathon then explained that the testimony was also offered because Marathon believed the County contended "there was a transfer point in the City of Chicago." *Id.* Counsel for the County responded, "Again, no argument that there was a delivery or a transfer point in Chicago." *Id.* These statements are directly contrary to the County's argument before this Court that the transactions provided for "the sale and delivery of fuel to Chicago, Illinois, in the heart of Cook County." *See* County's Br. at 55.

Given the County's inability to demonstrate a failure of proof on this issue, Marathon renews its legal arguments regarding extraterritoriality as stated in its opening brief and also refers the Court to the arguments raised by the Illinois Chamber of Commerce in its Brief in Support of Marathon's appeal. *See* Marathon Br. at 29-31; Illinois Chamber Br. at 12-16.

## V. Marathon Established that the ALJ's Imposition of Penalties Was Against the Manifest Weight of the Evidence.

### A. The County's argument that the more stringent IRS standards governing abatement of penalties for reasonable cause apply is without merit

The County argues for the first time in its brief that the IRS's stringent criteria for establishing reasonable cause for abatement of penalties associated with failure to pay taxes applies here rather than its more lenient criteria governing reasonable cause for accuracy-related penalties. The IRS imposes two different penalties for failure to pay taxes under IRC Section 6651, neither of which are akin to the penalties imposed in this case. The first is a penalty for failure to pay tax that is shown to be due on a return,

which is clearly not relevant here as the amounts the County assessed were not shown on Marathon's returns. *See* IRS § 6651(a)(2). The second is a penalty for "failure to pay tax required to be shown on a return, which was not shown, within 21 calendar days (10 business days if the amount demanded is $100,000 or more) of the date of the IRS notice and demand for the tax." IRS § 6651(a)(3). This penalty only arises after a taxpayer has received a notice and demand to pay the taxes and fails to do so within the prescribed period, which did not occur in this case. Both of these "failure to pay" penalties will be abated if the taxpayer can establish that the taxpayer's failure to pay is due to reasonable cause and not due to willful neglect. IRC § 6651(a)(2) & (3). Reasonable cause for failure to pay exists if the taxpayer has made a showing that the taxpayer exercised ordinary business care and prudence in providing for payment of the liability and was nevertheless either unable to pay the tax or would suffer an undue hardship if the taxpayer paid the tax on the due date. 26 C.F.R. § 301.6651-1(c)(1).

The County's argument that the penalties assessed here are "failure to pay" penalties and that the reasonable cause standard associated with "failure to pay" penalties applies is without merit. In this case, Marathon filed monthly tax returns and paid the amount of Motor Fuel Tax shown on the returns, so this was not a case of failure to pay any Motor Fuel Tax or failure to pay the amount shown due on the returns. The County audited Marathon's monthly returns and determined that additional tax is due on Marathon's Book Out transactions, which Marathon believed were not subject to the Motor Fuel Tax. The County issued a "Notice and Determination and Assessment" that assessed tax on the Book Out transactions and included a 10% late payment penalty and 25% negligence and willfulness penalty. C 236. There was no demand for payment of

Motor Fuel that preceded that notice which would have allowed Marathon to pay the taxes and avoid the penalties. In fact, the notice that was issued was not a final assessment and such a notice allows the taxpayer to file a written protest and request a hearing to contest the assessment, which is what Marathon did. Where a taxpayer has contested an initial assessment, a final assessment is not issued until the matter has been litigated. *See* Ord. Sec. 34-67(c); 34-81(g)(2) & (3). A final assessment has not yet been issued to Marathon. Thus, the penalties assessed by the County cannot be considered as akin to "failure to pay" taxes.

The only authority the County cites for its argument that the reasonable cause standard for "failure to pay" taxes applies is *Trans-Serve, Inc. v. United States*, 521 F.3d 462, 470 (5th Cir. 2008). The *Trans-Serve* case lends no support to the County's position because the facts in that case are vastly different than the facts here. In that case, Trans-Serve paid federal employment taxes under the Federal Insurance Contributions Act ("FICA") and Federal Unemployment Tax Act ("FUTA") rather than the higher taxes the IRS Office of Appeals determined were required under the Railroad Retirement Tax Act ("RRTA") and the Railroad Unemployment Repayment Tax Act ("RURTA") (the "Railroad Acts"). 521 F.3d at 465. Importantly, the case did not involve an underpayment of taxes as Trans-Serve did not pay any Railroad Act taxes whatsoever. The IRS audited Trans-Serve five times, determining each time that Trans-Serve was an "employer" under the Railroad acts and thus had failed to pay the Railroad Acts taxes. *Id*. After each of the audits, the IRS gave Trans-Serve an examination report and a thirty-day letter stating the basis for the assessments of Railroad Act taxes and the time within which Trans-Serve could appeal. *Id.* Trans-Serve protested each examination report and

appealed each tax assessment through the IRS's administrative appeals process, losing four of the five appeals. *Id*. The IRS first demanded that Trans-Serve pay the taxes under the Railroad Acts, as is required before asserting penalties under IRC § 6651(a)(3), after the IRS Office of Appeals determined that Trans-Serve was a "railroad employer." *Id*. at 471. The failure-to-pay penalties at issue did not accrue until twenty-one days after that notice. *Id*. Trans-Serve did not pay the taxes within the specified period; thus the penalties were due. Trans-Serve is clearly distinguishable from the facts in this case as Marathon paid some Motor Fuel Taxes with its original returns and the County did not issue a demand for payment of taxes before imposing the penalties.

### B. The penalties should be abated under the IRS standards governing reasonable cause for underpayment of taxes

The penalties at issue are akin to the accuracy-related penalties imposed by the IRS under IRC Section 6662 and therefore the reasonable cause standards governing those penalties should apply here. The IRS imposes accuracy-related penalties under IRC Section 6662(b)(1) and (2) if a taxpayer's negligence or disregard of rules or regulations caused an underpayment of tax, or if an underpayment exceeded a computational threshold called a substantial understatement, respectively.[11] Negligence is defined to include "any failure to make a reasonable attempt to comply" with the provisions of the IRC, and the term "disregard includes any careless, reckless, or intentional disregard." IRC § 6662(c). One of the strong indicators of negligence includes where a taxpayer failed to ascertain the corrections of a deduction, credit, or exclusion. Treas. Reg. § 1.6662-3(b)(1)(i)-(ii). Generally, taxpayers are not subject to

[11] IRC Section 6662(b) also authorizes the IRS to impose five other accuracy-related penalties that are under a variety of circumstances that are not relevant here.

the accuracy-related penalties if they can establish that they had reasonable cause for the underpayment and acted in good faith. IRC § 6662(c)(1). The determination of whether a taxpayer acted with reasonable cause and in good faith is made on a case-by-case basis, considering all pertinent facts and circumstances. 26 CFR 1.6664-4(b). Circumstances given consideration in this assessment include an honest misunderstanding of fact or law that is reasonable in light of the experience, knowledge and education of the taxpayer. *Id*.

The late payment penalty and the negligence or willfulness penalty that the County assessed are akin to the accuracy-related penalties described in IRC Section 6662(b)(1). Marathon self-assessed and timely paid Motor Fuel Tax on its monthly total sales of product. The County audited Marathon's monthly Motor Fuel Tax returns and determined that Marathon should have paid tax on the monies it received from Book Out transactions. The County assessed penalties related to those underpayments of Motor Fuel Tax.

Marathon provided evidence to support abatement of penalties in full under the IRC's reasonable cause criteria for abatement of accuracy-related penalties. Notably, under the IRC, it is the IRS that bears the initial burden of production regarding the accuracy-related penalties. IRC § 7491(c). The IRS must first present sufficient evidence to establish that the penalty is warranted. The burden of proof then shifts to the taxpayer to establish any exception to the penalty, such as reasonable cause. IRC § 7491(a). Here the County did not present any evidence that the penalties are warranted. Nonetheless, Marathon introduced evidence at the hearing to support its claim that Marathon reasonably relied upon the plain language of the Ordinance when calculating its tax liability. As discussed in Section II.A., the plain language of the Ordinance

imposes the tax on retail sales of tangible product (i.e. gasoline or fuel). The Book Out transactions at issue here are strictly financial transactions which involve no physical transfer or change in ownership of gasoline or fuel. And as the appellate court recognized, "[n]o prior Illinois case established the taxability of book-out transactions as sales." A-18. Mr. Steiner, Marathon's motor fuel tax specialist, who was an employee in Marathon's tax and accounting departments for over 36 years, testified that his understanding of a retail sale involved physical movement of product and that he believed that Book Out transactions do not constitute retail sales because there is no physical movement of product to consumers. C 12694. Mr. Steiner further testified that Marathon had never been assessed tax on a Book Out transactions in any other jurisdiction. C 12691. Under these circumstances, it was reasonable for Marathon to conclude that the Book Out transactions are not subject to the Motor Fuel Tax. Thus, the penalties should be abated in full.

Despite the County's assertions to the contrary, the appellate court's reliance on *Horsehead Corp. v. Department of Revenue*, 2019 IL 124155 (2019), was not legal error. In *Horsehead*, this Court found that Horsehead had reasonable cause for failing to pay the tax because the exemption, which Horsehead argued was applicable to its case, had no statutory definition and no caselaw that Horsehead could rely on for guidance as to how the exemption is interpreted and applied. *Id.* ¶ 15. Accuracy-related penalties imposed under the IRC have been similarly abated where the taxpayer has shown that the state of the law was uncertain. In *Patel v. Comm'r*, 138 T.C. 395 (2012), the taxpayers claimed a charitable contribution when they donated their home to the local fire department for use in training exercises. The state of law regarding the type of ownership interest in the

house that the taxpayers transferred to the fire department was unsettled. The Tax Court denied the deduction but declined to impose the accuracy-related penalty because "[w]hen petitioners filed their return, the legal issues raised by their charitable contribution deduction claim were not settled." *Id*. at 417. Thus, there is no basis to conclude that the appellate court erred in applying that same analysis here.

For all of these reasons, this Court should affirm the appellate court's ruling that the imposition of penalties was against the manifest weight of the evidence.

## CONCLUSION

For all of the foregoing reasons and those discussed in Marathon's opening brief, this Court should void the Revised Assessment in its entirety and make the findings requested in Marathon's Opening Brief.

Dated: May 29, 2024

Respectfully submitted,

*/s/ Catherine A. Battin*

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## CERTIFICATE OF COMPLIANCE

Catherine A. Battin hereby certifies that this brief conforms to the requirements of Rules 341(a) and (b). The length of this reply and response brief, excluding the pages contained in the Rule 341(d) cover, the Rule 341(h)(1) table of contents and statement of points and authorities, the Rule 341(c) certificate of compliance, the certificate of service, and those matters to be appended to the brief under Rule 342(a), is 37 pages.

*/s/ Catherine A. Battin*
Catherine A. Battin

**NOTICE OF FILING and PROOF OF SERVICE**

In the Supreme Court of Illinois

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| MARATHON PETROLEUM, COMPANY LP f/k/a MARATHON PETROLEUM COMPANY, LLC, | ) | |
| *Plaintiff-Appellant/Cross-Appellee,* | ) | |
| v. | ) | No. 129562 |
| COUNTY OF COOK, COOK COUNTY DEPARTMENT OF REVENUE, et al., | ) | |
| *Defendants-Appellees/Cross-Appellants.* | ) | |

The undersigned, being first duly sworn, deposes and states that on May 29, 2024, there was electronically filed and served upon the Clerk of the above court the Appellant's Reply Brief and Response to Request for Cross-Relief. On May 29, 2024, service of the Reply / Response Brief will be accomplished through the filing manager, Odyssey EfileIL, to the following counsel of record:

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Within five days of acceptance by the Court, the undersigned states that 13 paper copies of the Reply / Response Brief bearing the court's file-stamp will be sent to the above court.

*/s/ Catherine A. Battin*
Catherine A. Battin

Under penalties as provided by law pursuant to Section 1-109 of the Code of Civil Procedure, the undersigned certifies that the statements set forth in this instrument are true and correct.

*/s/ Catherine A. Battin*
Catherine A. Battin