

apply for all periods open to adjustment. All references to section numbers are to the Wisconsin Statutes unless otherwise noted.)

SALES TAX

I. Coupons Issued by Manufacturers

Manufacturers frequently mail coupons to consumers which are redeemable for taxable merchandise (e.g., soap or paper products) or which may be used to purchase such merchandise at a reduced sales price at any retail store. The transfer of a bar of "free" soap or "discounted" soap to a customer by a retailer in exchange for a coupon issued by the soap manufacturer is considered a sale. The consideration for the sale upon which the sales tax is imposed is the amount the manufacturer reimburses the retailer plus the amount (if any) that the consumer pays when redeeming the coupon. This consideration constitutes taxable gross receipts of the retailer. For example, if the customer uses a 25¢ manufacturer's coupon and \$1.24 cash to purchase a box of soap with a retail price of \$1.49, the retailer has taxable gross receipts of \$1.49.

For additional information on this topic, see administrative rule Tax 11.28, entitled "Gifts, advertising specialties, coupons, premiums and trading stamps".

II. Industrial Gases Used by Manufacturers

Industrial gases purchased by a manufacturer for use as a fuel are subject to the sales or use tax. This includes a manufacturer's purchase of oxygen, acetylene or other gases for use as a fuel in welding torches. However, shielding gases which do not burn or provide a source of power are exempt, when consumed or destroyed by a manufacturer in the manufacture of tangible personal property destined for sale.

Even though the purchase of the gas may be exempt, the charge (sometimes called "demurrage") by the gas supplier for retention by the customer of gas cylinders is subject to the sales tax.

For additional information on this and related topics, see administrative rule Tax 11.81, entitled "Industrial gases, welding rods and fluxing materials".

III. Sandwiches, Heated Foods or Beverages

Gross receipts from sales of heated foods or heated beverages are taxable, regardless of whether the item purchased is consumed on or off the seller's premises. Thus, the tax applies when:

- a. A supermarket sells chicken or ribs roasted on a rotisserie.
- b. A bakery sells hot coffee.
- c. A fish market sells hot prepared fish.

REPORT ON LITIGATION

(This portion of the WTB summarizes recent significant Tax Appeals Commission and Wisconsin court decisions. In cases which decisions adverse to the Department's position are rendered, it will be noted whether or not the Department acquiesces or will appeal.)

Affiliated Bank of Middleton vs. Department of Revenue (Wisconsin Tax Appeals Commission, June 6, 1979.) Taxpayer held a sales tax seller's permit. It owned a building which was permanently attached to a cement foundation and had permanent water, sewer and electrical connections. The Commission stated that, for property taxation, the building was taxed as real property and not as personal property.

In September 1974, taxpayer agreed to sell the building to a savings and loan association for use at a different site as a branch building. Taxpayer employed a house mover who disconnected the permanent water, sewer and electrical connections, separated the building by hoisting it on a flat bed trailer and hauling it. At its new location, the building was immediately placed on a permanent cement foundation and permanent water, sewer and electrical connections were made. No wheels were ever attached to the building in the moving process. The purchase price represented the price of the building moved on the land of the purchaser.

The Department contended that the sale was a sale of tangible personal property subject to the sales tax. Taxpayer contended that the sale was of real property, not subject to the sales tax. The Commission held in favor of the taxpayer.

The Department has appealed this decision.

Burch Construction Co. vs. Department of Revenue (Wisconsin Tax Appeals Commission, May 31, 1979.) Taxpayer was in the business of constructing highways and sewers. In 1970, taxpayer's volume of highway construction business significantly declined due to diminished interstate highway construction. In 1972, taxpayer underbid a sewer construction project and incurred a \$400,000 loss. In June 1973, taxpayer auctioned off its surplus highway construction equipment grossing about \$351,000 which was distributed as follows: about \$3,700 as auction commission, about \$315,000 as payment of taxpayer's debts, about \$32,000 available for operations.

Taxpayer remained in the highway construction business after the auction with heavier emphasis on sewer construction. During each of its fiscal years covering the period 1968 to 1977, taxpayer purchased and sold a significant amount of construction equipment and auctions similar to its June 1973 auction were common in the construction industry. Taxpayer realized a capital gain on the June 1973 auction sale of its construction equipment, due in part to depreciation previously claimed. The auction was made for compelling business reasons and was attributable to the then present and continuing operations of taxpayer's business. On its 1973 Wisconsin income/franchise tax return, taxpayer carried forward losses from the previous 2 taxable years and offset them against the gain realized at the auction.

On June 30, 1973, taxpayer adopted a plan of partial liquidation under sections 331(a)(2) and 346 of the Internal Revenue Code. Under the plan, 60% of the outstanding capital stock of Burch Construction Company was redeemed by the corporation reducing the number of shareholders from 6 to 1. After the partial liquidation, taxpayer retained over \$300,000 in assets and remained active in the construction business. No auction proceeds were used to redeem corporate stock.

The Department disallowed the carry forward of the business losses from the 2 taxable years preceding 1973 because they were not "attributable to the operation of a trade or business regularly carried on by the taxpayer" (emphasis added) within the language of s. 71.06, Wis. Stats.

The Commission held in favor of the taxpayer. It concluded that taxpayer's construction equipment auction was for compelling business reasons and was attributable to the operation of its business; that taxpayer's gain from the sale of its construction equipment constitutes net business income under s. 71.06, Wis. Stats.; and that the taxpayer may carry forward its 2 net business losses from the 2 previous taxable years and offset them against the gain it realized in its 1973 equipment business auction.

The Department did not appeal this decision.

Department of Revenue vs. Family Hospital, Inc. (Circuit Court of Dane County, June 18, 1979.) Taxpayer is a nonprofit Wisconsin corporation organized exclusively for charitable, scientific and educational purposes. It operates a nonprofit hospital, the Family Hospital in Milwaukee. Taxpayer receives proceeds from the operation of its parking lot adjoining the hospital, used substantially by patients, employees and guests of the hospital.

The sole issue in this case was whether gross receipts from parking received by taxpayer are subject to the sales tax. The Tax Appeals Commission had determined that the taxpayer's gross receipts from parking were not subject to sales tax. The Department appealed that decision.

The Court upheld the Commission's conclusion and ruled in favor of the taxpayer. The Court stated that it is clear that taxpayer's receipts from its parking facility are subject to sales tax under s. 77.52 (2) (a) 9 unless exempted from the tax by some other statute. The Court stated, however, that the hospital's receipts from parking were exempt by s. 77.54 (9a).

The Department has appealed this decision.

Harold W. Fuchs Agency, Inc. vs. Department of Revenue (Wisconsin Court of Appeals, District IV, June 26, 1979.) Taxpayer is engaged in the sale and rental of photocopy machines and copy machine paper and equipment. One issue was whether taxpayer's moneys collected from users of its coin-operated photocopy vending machines located in city of Milwaukee public buildings are subject to the sales tax. Taxpayer placed

16 machines in city buildings as specified by its contract with the city, serviced the machines and collected the money from them, periodically accounted for the receipts to the city and paid the city 5.55¢ for each 10¢ copy made. The Appeals Court affirmed the Circuit Court and concluded that these gross receipts were subject to the sales tax, even though the premises on which the machines were placed were under the control of the city.

Taxpayer also contended that one machine located in the city hall was used by city employees which constituted an exempt sale to the city under s. 77.54 (9a). The Appeals Court agreed with the Circuit Court that no evidence was presented as to whether the city or its employees paid for or had the free use of the machine. Therefore, no portion of the machine's receipts were exempt under s. 77.54 (9a) as a sale to a city.

When the city of Milwaukee advertised for bids for the installation of the 16 photocopy machines, the invitation for bids indicated bids should be submitted without the Wisconsin sales tax, because the city is exempt from such tax. This provision was in every invitation for bids used by the city under a variety of circumstances, and was not applicable to this situation where the record failed to show that any receipts came from the city, the Appeals Court concluded.

The second issue was whether transportation charges collected by the taxpayer on intrastate shipments of tangible personal property were subject to the sales tax. These transportation charges were separately stated on the invoices issued to taxpayer's customers.

The Appeals Court affirmed the holding of the Circuit Court and stated that if the transportation charges were for transportation which occurred after the sale to the customer, such charges were not taxable under s. 77.51 (11) (b) 5, Wis. Stats. If these charges represent transportation which took place before the sale, they were subject to the tax under s. 77.51 (11) (a) 3, Wis. Stats.

Under s. 77.51 (4r), a sale occurs at the location of the customer when possession is transferred to the customer by the common carrier. Section 402.401 (2) (a), Wis. Stats., provided that a sale is completed as soon as a retailer delivers the purchased

property to a common carrier. Therefore, the Court had to determine which of these two conflicting statutes prevails to determine where a sale takes place for sales tax purposes. The Appeals Court affirmed the holding of the Circuit Court and found the sales and use tax law controls, and that the sale takes place at the location of the customer. Therefore, the transportation charges collected by the taxpayer from its customers on intrastate sales are subject to the sales tax.

Hide Service Corp. vs. Department of Revenue (Wisconsin Tax Appeals Commission, June 19, 1979.) Section 71.043, Wis. Stats., provides that sales and use taxes paid by a corporation on fuel and electricity consumed in manufacturing may be used to reduce income/franchise taxes payable for the year. This section indicates that "manufacturing" has the meaning designated in s. 77.51 (27)

(i.e., the production by machinery of a new article with a different form, use and name from existing materials by a process popularly regarded as manufacturing). The Department disallowed a reduction of the income/franchise taxes payable by the taxpayer on the grounds that taxpayer was not engaged in manufacturing.

Taxpayer was in the business of curing hides. The purpose of hide curing is to prevent deterioration of the hide and, through preservation, to increase the hide's usefulness by giving it the capacity to be transported long distances and stored for long periods of time.

Taxpayer uses the following machinery in its process: a fleshing machine, vibrating conveyors, screw conveyors, paddle wheels and a cylindrical washer. Taxpayer's procedure is the following: hides from slaughter houses are washed in water to remove dirt and debris; hides are soaked in a brine solution; hides are removed from the brine solution; flesh and fat are removed and the hides are trimmed, sorted, graded and stored until sold to tanners; and by-products of the taxpayer's products include waste for rendering and animal feed.

Taxpayer's hide curing process results in physical and biological changes in the hide which are irreversible. Prior to the application of taxpayer's process, the hides are called "green hides" and after the process they are called "cured hides"

as those terms are used in the hide and tanning industries. After application of taxpayer's process, cured hides have a different use than green hides as a result of the ability to transport them long distances and store them for indefinite periods of time.

The Tax Appeals Commission found that the taxpayer was engaged in manufacturing as that term is defined in s. 77.51 (27). As a result taxpayer could use sales taxes it paid during the year on fuel and electricity consumed in manufacturing to offset income/franchise taxes payable for the year.

The Department has appealed this decision.

Department of Revenue vs. Louis G. Shew (Circuit Court of La Crosse County, May 16, 1979.) Taxpayer purchased 2 securities after 1911 and prior to becoming a Wisconsin resident in 1974. The fair market value of the stocks had declined at the time taxpayer became a Wisconsin resident. The stocks declined further after taxpayer became a Wisconsin resident and he finally sold them.

For Wisconsin income tax purposes in reporting the loss on taxpayer's 1974 income tax return, taxpayer contended that the loss should be the difference between the stocks' purchase price and their sale price (i.e., the same as the federal loss). The Department contended that the loss should be the difference between the stocks' value at the time the taxpayer became a Wisconsin resident and their sale price. The Department's contention would result in a smaller loss (\$318.11) than the total loss contended for by the taxpayer (\$2,077.36). (The Department's position on this issue is contained in administrative rule Tax 2.97, "Sale of constant basis assets acquired prior to becoming a Wisconsin resident".)

The Tax Appeals Commission ruled in favor of the taxpayer. The Circuit Court sustained the conclusion of the Commission.

The Court concluded that the taxpayer's actual cost must be used by the Department in its income tax computations of gains and losses incurred by a Wisconsin resident-taxpayer on the sale of stock acquired after 1911 and not by gift. The Court said that Wisconsin should use federal definitions and computations as the foundation for the state income

tax on the sale of stocks by a Wisconsin resident.

The Department has appealed this decision.

Department of Revenue vs. Moebius Printing Co. and Moebius Printing Co. vs. Department of Revenue (89 Wis. 2d 610, Wisconsin Supreme Court, May 30, 1979.) Moebius is a printing and lithographing firm whose primary business is the sale of illustrated brochures, catalogs and folders which Moebius produces to special order. Moebius provided all the materials used in the printing involved in the sales in question and delivered all of the printed matter to its customers in Wisconsin.

In most of the sales involved in these cases, Moebius' customers executed exemption certificates. The purchasers checked the box before the line reading "Other purchases exempted by law (State items and exempt use)." Moebius' customers completed the line by stating that all or a specified percentage of the printed materials purchased was to be distributed outside of Wisconsin. In a few of the sales involved, similar statements were made by the purchasers in resale certificates or in letters.

During the time period involved—September 1, 1969 to December 31, 1971—the sales tax law did not contain such an exemption. (Such exemption was enacted, however, as s. 77.54 (25), effective May 22, 1972.) Moebius accepted the certificates and letters in the belief that the purchases covered by them were exempt from the sales tax.

In October 1970, James Lydon, a Department tax representative visited Moebius' office and examined their books and records for the month of August 1970. It appears that Moebius made available all of its sales records from September 1, 1969 to the date of the visit. However, there is no evidence that Mr. Lydon examined records for any month other than August 1970.

After his visit, Mr. Lydon wrote Moebius a letter, on plain paper and apparently typed by Mr. Lydon, dated October 9, 1970. Mr. Lydon wrote Moebius that his report to the Department "included" the statement that he had made a "spot check" of all accounts payable for August 1970. For every purchase, he

wrote, there had either been tax paid or "valid exemption certificates on file". Mr. Lydon concluded: "In my opinion Moebius is doing an excellent all around job in compliance with the Wisconsin sales tax law."

On July 7, 1972, the Department issued a sales and use tax assessment against Moebius covering the period September 1, 1969 to December 31, 1971. This was based on a field audit conducted in 1972. Moebius sought a redetermination.

Moebius petitioned the Tax Appeals Commission for review. The Commission concluded that the sales in question were subject to the sales tax, that no statutory exemption existed for them, that the exemption certificates were not valid because they did not on their face indicate a legal basis for the claimed exemption, and that Mr. Lydon's visit and subsequent letter constituted a field audit and determination for August 1970 (so that no additional field audit for that month can be made).

The Circuit Court reversed the Commission's order, exempting from the tax the disputed transactions, stating that the Legislature did not intend to subject to sales tax the transactions involved. The Court, however, upheld the portion of the Commission's order barring the Department from assessing Moebius for August 1970.

The Wisconsin Supreme Court addressed several *substantive issues* and held the following on these issues (all in favor of the Department's positions):

1. The transactions were taxable. The statute is clear and no exemption existed. Although there was a similar exemption from the use tax (for retention of tangible personal property in Wisconsin for subsequent transportation and later use solely outside Wisconsin—s. 77.51 (16)), this exemption does not justify the Court's reading into the statutes a similar sales tax exemption where there was none.

2. This interpretation of the statutes does not constitute a denial of equal protection of the law. There is a presumption of tax laws' constitutionality which had a rational basis. Moebius failed to prove beyond a reasonable doubt that the statute had no rational basis.

3 Acceptance of the exemption certificates did not make the transactions exempt where no statute exempted the transactions. The certificates on their face fail to state a legal basis for exempting the sales from the sales tax.

The Wisconsin Supreme Court addressed several *procedural issues* involving the manner in which the Department's tax representative inspected Moebius' records and the manner of his communicating the results of his inspection to Moebius. The Court's conclusions on each issue follow:

1. *Issue:* Did Mr. Lydon's "spot check" in October 1970 of Moebius' records constitute a field audit for the period September 1, 1969 to December 31, 1971 and did Mr. Lydon's October 9, 1970 letter constitute a "notice of determination"? *Holding:* Mr. Lydon's "spot check" of Moebius'

records constituted a field audit, but of the period August 1970 only, since there was no evidence that records from other time periods were examined. (The statutes, said the Court, authorize the Department to conduct either a "field audit" or "office audit", not a "spot check"; Mr. Lydon's activities most resemble a field audit.) While the letter did not meet all the statutory requirements (s. 77.59 (3)) of a "notice of determination", it was deemed such a notice because it was "in substantial compliance" with the statute.

2. *Issue:* Is the Department estopped (barred) from collecting the portion of contested sales tax based on sales made after Mr. Lydon examined Moebius' records in October 1970 and wrote Moebius that the exemption certificates which it had on file were valid? (In other words, did

the conduct of the Department through its agent cause the taxpayer to act in good faith in a certain way based on its reliance on the agent's letter?)

Holding: The Department is estopped from collecting sales tax based on its field audit from October 9, 1970, the date of Mr. Lydon's letter containing the representations upon which Moebius relied, to December 31, 1971. The Department is not estopped from collecting sales tax on sales prior to October 9, 1970 (except for August 1970). The majority of the Court believed that Moebius' reliance on Mr. Lydon's letter was reasonable and justifiable. Justice Abrahamson dissented from the majority opinion insofar as it concludes that Moebius relied upon the tax representative's letter and that the reliance was reasonable.