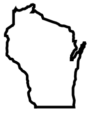

Report on Litigation

Summarized below are recent significant Wisconsin Tax Appeals Commission (WTAC) and Wisconsin Court decisions. The last paragraph of each decision indicates whether the case has been appealed to a higher Court.

The following decisions are included:

Individual Income Taxes

Business expenses – rent or lease expenses
Michael D. and Arthena K. Haza (p. 15)

Exclusions from gross income – trip received as gift
Gary J. Grow and Mary L. Schroeder. (p. 16)

Indebtedness discharge
Ronald J. and Mary Anne Hintzke (p. 16)

Individual Income Taxes, and Sales and Use Taxes

Assessments –net worth
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Penalties – fraud, false or fraudulent return
Don Ahn, Don and Louise Ahn, and Don Ahn d/b/a Don's Pub (p. 17)

Homestead Credit

Property taxes accrued – property owned by partnership
Edwin L. and Dorothy V. Sanftner, Leo E. and Sally L. Sanftner, and Peter G. and Donna M. Kreft (p. 19)

Corporation Franchise and Income Taxes

Insurance companies – interest from United States obligations
American Family Mutual Insurance Company and American Standard Insurance Company of Wisconsin (p. 20)

Reorganizations – stepped-up basis of assets
The Toro Company (p. 20)

Corporation Franchise and Income Taxes, and Sales and Use Taxes

Gross income – gross receipts
Greenwood Hills Country Club (p. 21)

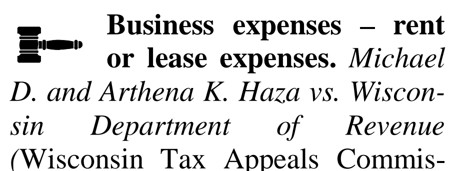
Sales and Use Taxes

Motor vehicles and trailers – nonresident purchases
Johnson Welding & Mfg. Co., Inc., a/k/a Johnson Truck Bodies (p. 22)

Sales and Use Taxes, and Withholding of Taxes

Officer liability
Donald D. Noard (p. 22)

INDIVIDUAL INCOME TAXES



Business expenses – rent or lease expenses. *Michael D. and Arthena K. Haza vs. Wisconsin Department of Revenue (*Wisconsin Tax Appeals Commission, January 7, 1999). The issue in this case is whether business expenses for rent or lease of other business property were properly deducted.

Taxpayer Michael D. Haza and another lawyer, Mr. Arik J. Guenther, own Guenther & Haza, Ltd. ("the firm"), a Wisconsin corporation. In essence, the firm serves as a flow-through entity by which Messrs. Haza and Guenther ("the owners") made expenditures necessary to their respective law practices.

Each month, the owners each pay one-half of certain operating expenses for the firm, including supplies, staff salaries, utilities, and rent. In addition, each month the owners pay 100 % of the cost advances made by the firm for each of their respective clients. All receipts were paid directly to the lawyer who performed the services, not to the firm.

For the years at issue (1990 to 1992), the taxpayers claimed Mr. Haza's payments to the firm as rent or lease of other business property. The amounts claimed were $48,801 in 1990, $50,016 in 1991, and $49,203 in 1992.

In March 1996, the department issued two separate income tax assessments against the taxpayers, one for 1990 and the other for 1991, 1992, and 1994. The department granted the taxpayers' petition for review with regard to 1994 but denied the petition for review with regard to 1990 to 1992.

Following trial, the department conceded that the taxpayers should be allowed to deduct rent or lease expenses of $38,689.08 for 1990, $45,295.99 for 1991, and $41,886.85 for 1992.

The Commission concluded that the taxpayers should be allowed to deduct the amounts conceded by the department. The taxpayers may not claim any amounts in excess of those amounts, because they did not present consistent documentary evidence to support the higher amounts claimed.

Neither the department nor the taxpayers have appealed this decision. □

Exclusions from gross income – trip received as gift. *Gary J. Grow and Mary L. Schroeder vs. Wisconsin Department of Revenue* (Wisconsin Tax Appeals Commission, January 4, 1999). The issue in this case is whether two trips given to the taxpayers were taxable business promotions or nontaxable personal gifts.

During the years at issue (1992 and 1993), Taxpayer Mary L. Schroeder owned and was president of Miller Homes, Inc. ("Miller") – a corporation in the home construction business. Her husband, taxpayer Gary J. Grow, was not associated with Miller.

During those years, Mr. Grow's brother-in-law, Jim Curtes, was president of Auer Steel & Heating Supply Company ("Auer"). Among other things, Auer distributed Bryant and Carrier brand heating and cooling systems to dealers that sold and installed these systems. Auer supplied all such units in the geographic area in which Miller operated.

In 1992, Auer sponsored a trip to Cancun for certain Carrier brand dealers that sold and installed these systems supplied by Auer. Auer also sponsored a trip to San Diego in 1993, for certain Bryant dealers that sold and installed these systems supplied by Auer. In both instances, dealers were invited on the trip if they met certain sales criteria.

Because there was space available on both trips, Mr. Curtes invited the taxpayers to join the excursions in 1992 and 1993. The invitations were personal, not a promotion on Auer's part. Auer paid for the cost of both trips for the taxpayers, as well as the Carrier dealers in 1992 and the Bryant dealers in 1993.

The taxpayers did not report the cost of either trip on their income tax returns for 1992 and 1993. Auer did not send a Form 1099 with respect to the cost of the trips.

As a result of an audit by the department, in 1996 Auer informed participants in the two trips of the cost of each trip - $2,600 for the Cancun trip and $2,160 for the San Diego trip. The department assessed the taxpayers for additional income taxes for 1992 and 1993, based on the value of the two trips. The basis for the assessment was that the trips were received by Miller and passed on to the taxpayers.

The Commission concluded that the taxpayers are not liable for income tax on the value of the two trips, because the trips were gifts made to the taxpayers, not to Miller. Miller is not a dealer for either Bryant or Carrier and cannot purchase such products directly from Auer. In addition, Jim Curtes customarily included his personal friends and relatives on trips such as the ones at issue, and it is reasonably clear that the taxpayers received these gifts out of the generosity of Mr. Curtes.

The department has not appealed this decision.

CAUTION: This is a small claims decision of the Wisconsin Tax Appeals Commission and may not be used as a precedent. This decision is provided for informational purposes only. □

Indebtedness discharge. *Ronald J. and Mary Anne Hintzke vs. Wisconsin Department of Revenue* (Wisconsin Tax Appeals Commission, December 15, 1998). The issue in this case is whether the amount of a discharged debt was properly added to the taxpayers' income for 1992.

In 1990, Ronald J. Hintzke ("the taxpayer") entered into a contract with United Group Association, Inc. ("UGA"), concerning the sale of health insurance plans and policies. Under the contract, the taxpayer was a district manager who was responsible for the activities of certain "sub-members."

In the course of selling health insurance policies or plans, certain of the taxpayer's sub-members became indebted to UGA or ran a "debit balance." Such debit balances typically occurred when a customer prematurely cancelled a plan or policy for a period for which the sub-member had already been paid compensation. With regard to these debit balances, the contract provided, in part, that in consideration for the taxpayer's appointment as a district manager, and the benefits to be derived, he guaranteed payment of each sub-member's debit balance.

One or more of the taxpayer's sub-members resigned during his tenure as a district manager and left him responsible for their debit balances. Ultimately, the contract was terminated, and, under the terms of the contract, the taxpayer owed UGA $7,398. In 1992, UGA forgave this debt. The taxpayers did not report any portion of this discharged debt as income.

In January 1997, the department issued an income tax assessment against the taxpayers for 1992 and 1993. The assessment involved a number of issues, including the fail-

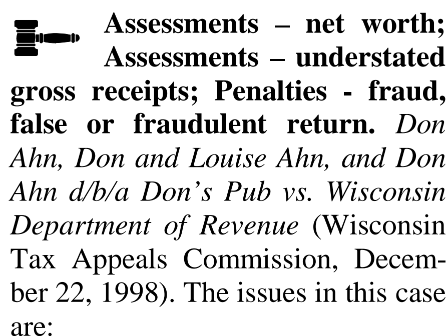
ure to report the discharged debt as income. The taxpayers filed a timely petition for redetermination, objecting only to that portion of the assessment concerning the discharged debt. The department denied the petition for redetermination, and the taxpayers filed a timely petition for review with the Commission.

The taxpayers argued that the discharged debt should not be treated as taxable income, because the taxpayer was only the guarantor of the debt and did not realize an increase in his net worth as the result of the original indebtedness. They also argued that the discharged debt is exempt under IRC secs. 108(a)(1)(C), which exempts qualified farm indebtedness from gain recognition, and 108(c)(2), which deals with the exemption for discharge of qualified real property business indebtedness.

The Commission concluded that the department properly added back the amount of the forgiven debt, because such amount is gain not otherwise excluded or deductible under Chapter 71 or the Internal Revenue Code. The taxpayer received something in exchange for his guarantee of the debt: he was named a district manager and was entitled to the benefits that accompanied that appointment. The debt does not qualify for exemption under IRC sec. 108(a)(1)(C), because (1) the debt was not incurred in the "trade or business of farming," and (2) the record fails to show that for the three years preceding 1992, 50% or more of the taxpayer's gross receipts was from the trade or business of farming. Finally, IRC sec. 108(c)(2) was not in effect at the time of the discharge in this case (the change took effect with discharges after December 31, 1992), and moreover, this provision only applied to indebtedness related to real property. The taxpayers have not appealed this decision.

CAUTION: This is a small claims decision of the Wisconsin Tax Appeals Commission and may not be used as a precedent. This decision is provided for informational purposes only. □

INDIVIDUAL INCOME TAXES, AND SALES AND USE TAXES



Assessments – net worth; Assessments – understated gross receipts; Penalties - fraud, false or fraudulent return. *Don Ahn, Don and Louise Ahn, and Don Ahn d/b/a Don's Pub vs. Wisconsin Department of Revenue* (Wisconsin Tax Appeals Commission, December 22, 1998). The issues in this case are:

A. Whether two income tax assessments covering the periods 1979 through 1985 and 1986 through 1989 are correct.

B. Whether fraud penalties imposed on the two income tax assessments are correct.

C. Whether a sales and use tax assessment covering the period 1984 through 1989 is correct.

D. Whether the fraud penalty imposed on the sales and use tax assessment is correct.

In December 1991, the department assessed taxpayer Don Ahn for additional income tax, plus interest and penalties, for 1979 through 1985. The department also assessed Don and Louise Ahn for additional income tax, plus interest and penalties, for 1986 through 1989. Both adjustments for additional income were derived from the department's reconstruction of income based upon the net worth method of audit.

As part of both assessments, the department added a fraud penalty based on its assertion that the taxpayers filed incorrect returns with the intent to defeat or evade income taxes. The fraud penalty equaled 50% of the additional income tax assessed for 1979 through 1984, and 100% of the additional income tax assessed for 1985 through 1989.

Also in December 1991, the department assessed taxpayer Don Ahn d/b/a Don's Pub for sales and use tax, plus interest and penalty, for 1984 through 1989. As part of that assessment, the department added a 50% fraud penalty based on its assertion that the taxpayer filed false or fraudulent returns with intent to defeat or evade the sales and use tax.

The taxpayers filed a petition for redetermination relating to each of the three assessments, objecting to the assessments. The department granted in part and denied in part each petition for redetermination. The taxpayers filed a timely petition for review appealing each of the department's actions on the petitions for redetermination.

During the eleven-year period under review, Don Ahn owned various income-producing properties and operated certain businesses, including at various times two coin laundries, a video game arcade, and two taverns. In 1982, he built a commercial building. In tax returns after the building was built, he used a basis of $50,000 for depreciation.

The taxpayer also owned a four-unit residential apartment building. Typically, he would deposit rent checks for three of the units in an account established for the apartment building and would cash the fourth check to use the proceeds apparently for the apartment building.

Don Ahn was the sole owner of these various business enterprises and was responsible for their operation. During the period under review, Louise Ahn was employed as a high school teacher.

Ten of the taxpayers' eleven income tax returns for the period under review were received by the department after their original due dates, including the 1983 return received nearly four years late.

Don Ahn did not apply for a seller's permit until October 1987. He failed to file any sales tax returns until June 1988.

As part of the income reconstruction, the department sent to the taxpayers eleven cost of living schedules, explained the net worth method of audit, and requested that one schedule be completed for each year covered by the audit. The taxpayers failed to complete the schedules, and the department therefore estimated the taxpayers' cost of living for the years at issue. As part of the net worth calculation, the department assumed an opening net worth of $1,000 (assuming a larger opening net worth would have the effect of reducing the income subsequently assessed).

With respect to determining the correctness of the income tax portion of the assessments for the years 1983 through 1989, the taxpayers bear the burden of showing that the assessments are not correct. With respect to determining the correctness of the income tax portion of the assessments for 1979 through 1982, and with respect to the fraud penalties for all years, the department bears the burden of showing by clear and convincing evidence that the taxpayers intended to defeat or evade the income tax.

With respect to determining the correctness of the tax portion of the sales and use tax assessment, the taxpayers bear the burden of showing that this assessment is incorrect. However, with respect to the 50% fraud penalty, the department bears the burden to show by clear and convincing evidence that the taxpayers intended to evade or defeat the sales tax.

In response to the opening net worth assumption of $1,000, Don Ahn testified that he entered the audit period with between $50,000 and $100,000, including a $10,000 loan, $25,000 from the sale of an apartment building, and an unspecified amount of cash given to him from his father. Louise Ahn confirmed that prior to 1979, Don Ahn sold the apartment building for $25,000 and received a $10,000 loan. The department offered no evidence to contradict her testimony.

Don Ahn advised the department that he routinely withheld 10-15% of the receipts from his businesses for personal use. The department added income to account for underreporting by 12.5%, assuming that this income was added to his net worth, not used for personal expenses. The taxpayers argued that the additional income should not be added to net worth, but that it should be assumed that all of the additional income associated with this 12.5% was spent for personal use each year.

In the net worth schedule for 1982 and thereafter, the department used $50,000 as the basis in the restaurant building built that year, based on Don Ahn's 1982 income tax return. The taxpayer testified that he only invested about $35,000 in the construction of the building, and that a tenant paid for $15,000 in improvements. He failed to provide any documentation or corroborating evidence to support his testimony.

The department's auditor estimated the living expenses for the taxpayers based upon his recollection of the expenses of his own family during a similar period. The taxpayers submitted an exhibit listing their estimated personal living expenses for each year under review. This testimony was considered by the Commission to be very credible.

The department's assessment assumes certain college expenses incurred by the taxpayers, based upon the personal experience of the department's auditor. The department subsequently agreed that the costs for tuition, books, and room and board should be those listed on an Exhibit excerpted from the University of Wisconsin almanac.

The department listed a 1986 truck with a value of $10,844 as part of its net worth calculation. The taxpayers argued that the truck was wrecked in an 1988 accident, and that Don Ahn collected an undetermined amount of insurance proceeds.

With respect to the sales and use tax assessment, the department asserts that not only did the taxpayers understate their income for purposes of the income tax, but Don Ahn also understated his gross receipts for purposes of the sales and use tax. However, the taxpayer argued that there is no evidence to tie unreported income to his trade or business that was subject to the sales or use tax.

The Commission concluded as follows:

A. The two income tax assessments covering the periods 1979 through 1985 and 1986 through 1989 are correct, except for the following modifications:

   - The assessments are recalculated with regard to each of the years at issue, incorpo-

rating an opening net worth of $35,000.

- For each of the years 1979 through 1982 (the years for which the department bears the burden of proof) the income generated by the 12.5% assumption of receipts withheld was spent for personal use, not added to net worth.

- The assessments are modified to incorporate the personal living expenses as listed by the taxpayers.

- The assessments are modified to use the college expenses as listed in the exhibit from the University of Wisconsin almanac.

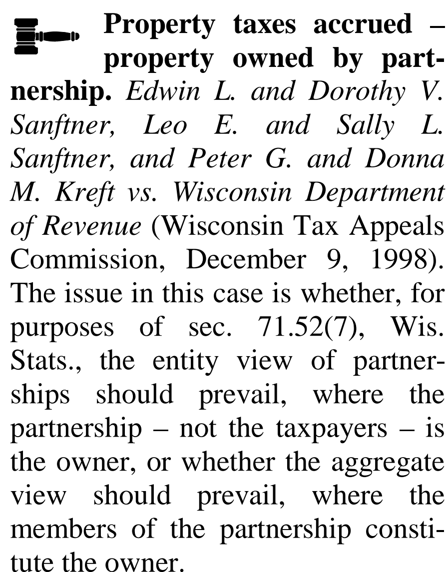
B. Fraud penalties were properly imposed on both of the income tax assessments. The department has met its burden of proof by showing that Don Ahn consistently underreported his income by 10-15%, and by the taxpayers' consistent tardiness in filing income tax returns.

C. The sales and use tax assessment is correct, except that it is modified consistent with the modifications to the two income tax assessments.

D. The fraud penalty was properly imposed on the sales and use tax assessment. The record is clear that Don Ahn routinely underreported his income by 10-15% per year, and he also failed to report those receipts for purposes of the sales and use tax. Moreover, he failed to apply for a seller's permit until 1987 or file sales tax returns until 1988.

Neither the department nor the taxpayers have appealed this decision. ☐

HOMESTEAD CREDIT



Property taxes accrued – property owned by partnership. *Edwin L. and Dorothy V. Sanftner, Leo E. and Sally L. Sanftner, and Peter G. and Donna M. Kreft vs. Wisconsin Department of Revenue* (Wisconsin Tax Appeals Commission, December 9, 1998). The issue in this case is whether, for purposes of sec. 71.52(7), Wis. Stats., the entity view of partnerships should prevail, where the partnership – not the taxpayers – is the owner, or whether the aggregate view should prevail, where the members of the partnership constitute the owner.

In June of 1979, the taxpayers executed and recorded a land contract under which they agreed to purchase a 120-acre farm in St. Croix County. Under the land contract, each couple own a 1/3 undivided interest in the property as joint tenants.

Also in June of 1979, the taxpayers formed a general partnership called Golden Maples Polled Hereford Haven. The partnership agreement provided that each of the six partners would share equally in profits, losses, and salary. In August of 1982, the taxpayers assigned their purchasers' interest in the land contract to the partnership, and apparently during the periods at issue the purchasers' interest in this land contract continues to be held by the partnership.

Each of the taxpayers resides in residences located on the parcel that is the subject of the 1979 land contract. The partnership pays the property taxes on the parcels and residences at issue.

Edwin and Dorothy Sanftner claimed and were paid homestead tax credits for 1994 and 1995. Leo and Sally Sanftner claimed and were paid homestead tax credits for 1993, 1994, and 1995. Peter and Donna Kreft claimed and were paid a homestead tax credit for 1994.

Under the date of June 30, 1997, the department assessed all three couples for most of the homestead tax credit that was claimed and paid. The bases for the assessments are that the property for which the homestead tax credit is claimed is not owned by the taxpayers, but rather by the partnership. In each case, the department allowed a portion of the property taxes paid, as rent.

The taxpayers all filed timely petitions for redetermination, and the department denied the petitions. All three couples filed timely petitions for review with the Commission.

The Commission concluded that the taxpayers are entitled to homestead tax credits for the years at issue, because the nature of their partnership interest is such that they are owners of the property for purposes of sec. 71.52(7), Wis. Stats. For purposes of the income tax, a general partnership is considered a pass-through entity, where income and other tax attributes flow to the individual partners. It would be unreasonable to construe ownership to mandate the entity view of general partnerships for purposes of sec. 71.52(7), Wis. Stats., when for other purposes the income tax treats general partnerships as aggregates.

The department has not appealed this decision.

CAUTION: This is a small claims decision of the Wisconsin Tax Appeals Commission and may not be used as a precedent. This decision is provided for informational purposes only. ☐

CORPORATION FRANCHISE AND INCOME TAXES

Insurance companies - interest from United States obligations. *American Family Mutual Insurance Company and American Standard Insurance Company of Wisconsin vs. Wisconsin Department of Revenue* (Wisconsin Supreme Court, December 16, 1998). This is a review of an October 30, 1997, decision of the Court of Appeals. See *Wisconsin Tax Bulletin* 107 (April 1998), page 13, for a review of that decision. The Court of Appeals reversed an order of the Circuit Court, which affirmed a decision of the Wisconsin Tax Appeals Commission upholding the Wisconsin franchise tax.

The single issue in this case is whether the Wisconsin franchise tax, secs. 71.43(2) and 71.45(2)(a)3, Wis. Stats. (1987-88), is a "nondiscriminatory franchise tax" within 31 U.S.C. sec. 3124(a)(1). If so, interest income from federal obligations may be included in the calculation of the Wisconsin franchise tax. A state franchise tax is discriminatory under federal law if interest income from federal obligations is included in the calculation but interest income from state or local obligations is excluded.

The taxpayers assert that they need not include interest income from federal obligations in calculating the franchise tax because the state excluded interest income from several state or local obligations in calculating the franchise tax. They further assert that to the extent that the Wisconsin franchise tax is calculated on the basis of interest income from federal obligations, the tax is invalid as violating a federal statute and the supremacy clause of the U.S. Constitution.

The Wisconsin Supreme Court concluded that the Wisconsin franchise tax is a "nondiscriminatory franchise tax" within 31 U.S.C. sec. 3124(a)(1). In the context of sec. 71.45(2)(a), Wis. Stats. (1987-88), and 31 U.S.C. sec. 3124(a)(1), interest income from obligations authorized under the bond statutes in question is to be included in the calculation for franchise tax purposes, regardless of how the interest income is treated for income tax purposes.

The Wisconsin Supreme Court reversed the decision of the Court of Appeals and remanded the case for further proceedings.

The taxpayers have not appealed this decision. □

Reorganizations - stepped-up basis of assets. *The Toro Company vs. Wisconsin Department of Revenue* (Wisconsin Tax Appeals Commission, December 11, 1998). The issues in this case are:

A. Whether sec. 71.337(1), Wis. Stats. (1985-86), requires Toro-Minnesota to recognize a gain in connection with a reorganization, which operates to increase the basis of the taxpayer's assets.

B. Whether sec. 71.362(2), Wis. Stats. (1985-86), requires the taxpayer to use as the basis of its assets the basis that Toro-Minnesota had in these same assets.

The taxpayer designs, manufactures, and markets consumer and commercial lawn maintenance equipment, snow removal equipment, and turf irrigation systems. During the years at issue, the taxpayer owned and operated a manufacturing plant located in Tomah, Wisconsin.

The Toro Company was incorporated in Minnesota in 1935 ("Toro-Minnesota"). In 1983, a "Merger Agreement" was filed with the Minnesota and Delaware Secretaries of State, to change the state of incorporation from Minnesota to Delaware. The change was completed through a reorganization under sec. 368(a)(1)(F) of the Internal Revenue Code ("IRC") and sec. 71.368(1)(a)6, Wis. Stats. Under the Merger Agreement, the merger of Toro-Minnesota resulted in the dissolution of Toro-Minnesota.

On the effective date of the merger, December 7, 1983, each share of Toro-Minnesota common stock issued and outstanding immediately prior to the merger (other than those shares with respect to which dissenters' rights were exercised and perfected) was converted into one share of the taxpayer's common stock. A holder of shares of Toro-Minnesota common stock had the right to receive payment of the "fair value" of the holder's shares of the stock in lieu of receiving shares of the taxpayer's common stock. Only one or two shareholders opted to do so.

Since the merger was effectuated through a reorganization under IRC sec. 368(a)(1)(F), pursuant to federal law, the taxpayer assumed the tax attributes of Toro-Minnesota. The department disallowed the taxpayer's assumption of Toro-Minnesota's Wisconsin tax attributes, specifically, Toro-Minnesota's Wisconsin net operating loss and manufacturer's sales tax credit carryforwards for the years ending 1984 through 1988. The taxpayer filed a timely petition for redetermination.

The department denied the petition for redetermination, claiming that when Toro-Minnesota merged with the taxpayer, the separate corporate

existence of Toro-Minnesota ceased, and, therefore, the net operating losses and manufacturer's sales tax credits were not transferable to the taxpayer under applicable Wisconsin law. The department's action in acting on the petition for redetermination as it pertains to the "intercompany expense allocation" was modified as set forth in a schedule attached to a partial stipulation dated October 8, 1997.

The taxpayer filed a Wisconsin franchise tax return for the fiscal year ending July 27, 1984, which included a notice that it had accomplished the reorganization under IRC sec. 368(a)(1)(F). The notice did not make any reference to a liquidation involving Toro-Minnesota or the taxpayer. The taxpayer did not file a plan of liquidation with the department, but at some point it did file the Merger Agreement with the department.

Toro-Minnesota and the taxpayer did not take certain steps that would most likely have occurred had the transaction at issue been a liquidation.

- Retained earnings of Toro-Minnesota were not distributed to shareholders, but rather passed on to the taxpayer;
- Toro-Minnesota did not recapture any portion of previously claimed accelerated depreciation and report it as income;
- Toro-Minnesota did not recapture any portion of its LIFO reserve and report this as income;
- Toro-Minnesota did not distribute its assets to shareholders or sell its assets and distribute the proceeds to shareholders.

The Commission concluded as follows:

A. The transaction at issue was not a liquidation under sec. 71.337(1), Wis. Stats. (1985-86). The requirement that assets be distributed in sec.71.337(1) means distribution to shareholders, not a transfer of assets to a successor corporation.

B. Under the plain language of sec. 71.362(2), Wis. Stats. (1985-86), assets in the taxpayer's hands have the same basis as they had in the hands of Toro-Minnesota. Section 71.362(2) unambiguously prohibits a step-up in basis for assets that are transferred in a reorganization such as the transaction at issue here.

The department is required to modify its action on the petition for redetermination as provided in the October 8, 1997, partial stipulation.

Neither the taxpayer nor the department has appealed this decision. □

CORPORATION FRANCHISE AND INCOME TAXES, AND SALES AND USE TAXES

Gross income–gross receipts. *Greenwood Hills Country Club vs. Wisconsin Department of Revenue* (Wisconsin Tax Appeals Commission, December 7, 1998). The issues in this case are whether 100% of the initial membership fees received by Greenwood Hills Country Club ("the corporation") are:

1. gross income for franchise and income tax purposes, and

2. gross receipts for sales and use tax purposes.

The corporation was organized in 1990 and is primarily engaged in the operation of a golf course and related facilities. Starting in 1991, the corporation sold initial memberships in the golf course club. One of the benefits to a member was the option of later returning the membership to the corporation and receiving a 75% refund of the cost. The corporation had unrestricted use of the initial membership fees that it received during the time at issue, and it used those fees to construct and operate the golf course and related facilities. Construction of the golf course began in 1992, and the course was completed in 1993.

Without owning an initial membership (or receiving an assignment of another's initial membership rights), a person cannot have the right to pay the annual fees to golf or use any of the other related facilities of the club. Inactive status is available to all who hold membership certificates. Inactive members pay no annual fees and cannot use any of the club's facilities. Memberships held as inactive might be held for investment purposes.

The corporation reported 25% of the total initial membership fees it received as gross income for franchise and income tax purposes. Likewise, the corporation only reported to the department sales tax on 25% of the total initial membership fees it received. The department imposed Wisconsin corporate franchise or income tax as well as Wisconsin sales tax on the remaining 75% of the initial membership fees received by the corporation.

The Commission concluded that the department was correct in its imposition of franchise or income and sales tax. All of the initial membership fees at issue were gross income at the time they were received by the corporation; therefore, the corporation was not entitled to exclude from its current income the 75% portion subject to refund at a later date. The fees were also subject to sales tax under sec. 77.52(2)(a)2, Wis. Stats.,

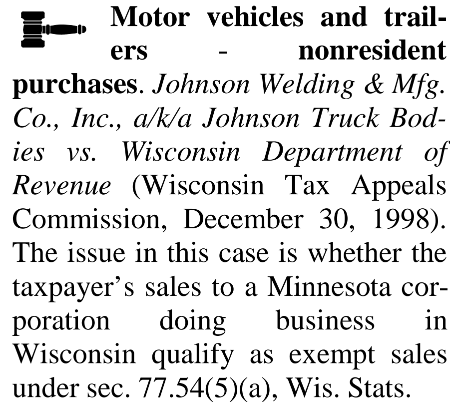
when they were received; the corporation was not entitled to exclude from the current measure of tax the 75% portion subject to refund at a later date.

1. Income from memberships is gross income because it was derived from the corporation's golf course business, unless there is an exception specifically provided elsewhere in the Internal Revenue Code. The Commission rejected the corporation's argument that the corporation uses the accrual method of accounting and the income is properly accounted for as of a different period under section 451 of the Code. The corporation was not prevented from using the entire fee income in its business operations. The Commission ruled that the income must be reported in gross income "when all the events have occurred which fix the right to receive such income and the amount thereof can be determined with reasonable accuracy" per Treas. Reg. Sec. 1.61-1.

2. The corporation disputed the imposition of the sales tax on the receipts on the grounds that payment of the initial membership fee provided access to nothing until and unless the required annual fee was paid. Without paying the initial fee, however, there was no access. The Commission determined that both the initial fee and annual fee were clearly for the furnishing of the privilege of access to the golf course and related club facilities.

The taxpayer has not appealed this decision. □

SALES AND USE TAXES



Motor vehicles and trailers - nonresident purchases. *Johnson Welding & Mfg. Co., Inc., a/k/a Johnson Truck Bodies vs. Wisconsin Department of Revenue* (Wisconsin Tax Appeals Commission, December 30, 1998). The issue in this case is whether the taxpayer's sales to a Minnesota corporation doing business in Wisconsin qualify as exempt sales under sec. 77.54(5)(a), Wis. Stats.

During the month of January 1997, the taxpayer sold 28 truck bodies to Schwan's Sales Enterprises, Inc. ("Schwan's") and delivered the truck bodies to Schwan's plant located in Rice Lake, Wisconsin. The taxpayer charged and collected 5.5% Wisconsin state and county sales tax on all 28 truck bodies it sold to Schwan's and remitted such tax to the department. Three of these truck bodies were installed on trucks assigned by Schwan's to Schwan's depots located in Wisconsin. The other 25 truck bodies were installed on trucks assigned by Schwan's to Schwan's depots located in other states.

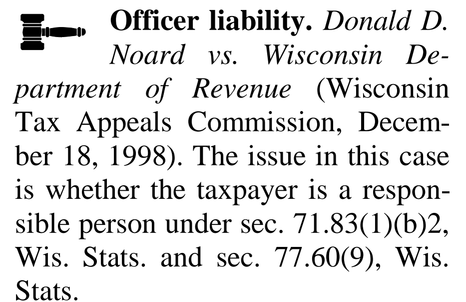
Schwan's is a corporation organized and incorporated under the laws of Minnesota. Its corporate headquarters are, and at all time during its existence have been, in Minnesota. Schwan's does business in all 50 states, including permanent places of business at 19 locations throughout Wisconsin.

Schwan's requested a refund from the taxpayer for sales tax paid on the 25 non-Wisconsin truck bodies. The basis of their refund request was that the truck bodies are exempt under sec. 77.54(5)(a), Wis. Stats., because they were sales made to a person who is not a resident of Wisconsin and who will not use the trucks for which the truck bodies were made otherwise than in their removal from Wisconsin. The taxpayer prepared and filed a claim for refund with the department.

The Commission concluded that the taxpayer's sales to Schwan's qualified for the sales tax exemption in sec. 77.54(5)(a), Wis. Stats. The Commission stated that no provision exists in Chapter 77, which covers Wisconsin sales and use taxes, that would include a Minnesota corporation as a Wisconsin "resident" for sales tax purposes.

The department has appealed this decision to the Circuit Court. □

SALES AND USE TAXES, AND WITHHOLDING OF TAXES



Officer liability. *Donald D. Noard vs. Wisconsin Department of Revenue* (Wisconsin Tax Appeals Commission, December 18, 1998). The issue in this case is whether the taxpayer is a responsible person under sec. 71.83(1)(b)2, Wis. Stats. and sec. 77.60(9), Wis. Stats.

Wis-Que, Inc. ("the corporation"), a Wisconsin corporation, was organized in 1983 with the objective to own and operate Larry's Texas Style BBQ, a sports bar and restaurant ("the restaurant"). The taxpayer's son, Jeffrey Noard, was listed as the vice president and secretary of the corporation, as well as one of its directors.

In early October 1994, Jeffrey Noard asked the taxpayer to evaluate the prospects of the restaurant. Two weeks later the taxpayer was asked to become involved in several aspects of the business: determine its viability; look at the books; make recommendations regarding customer service; and then to consult with some of the directors. Soon afterward the taxpayer began making

regular trips from his home in Milwaukee to the restaurant in Green Bay, as often as six days a week.

The taxpayer participated in restaurant meetings, direct negotiations with vendors, scrutiny of the restaurant's daily revenues, as well as various other duties. The taxpayer was involved in the corporation's checking accounts, savings account, and credit card operations. The taxpayer maintained a close relationship with the restaurant until it closed in January of 1995.

The Commission concluded the taxpayer was a responsible person under both sec. 71.83(1)(b)2, Wis. Stats. and sec. 77.60(9), Wis. Stats. The taxpayer had the authority and the duty to pay the company's withholding and sales tax liabilities, but he intentionally breached his duty.

The taxpayer received authorization from the restaurant's directors to take charge of the daily operations of the restaurant. He was given the **authority** to run the business. Once the taxpayer had the authority, he had a **duty** to comply with the law. He understood the tax situation but did not correct it. A person who is either given or assumes authority to operate a business has a duty to see that the business satisfies its tax obligations. The taxpayer **intentionally breached his duty** because he failed to file tax returns on a timely basis and failed to pay the corporation's tax liabilities.

The taxpayer has not appealed this decision. □

Tax Releases

"Tax releases" are designed to provide answers to the specific tax questions covered, based on the facts indicated. In situations where the facts vary from those given herein, the answers may not apply. Unless otherwise indicated, tax releases apply for all periods open to adjustment. All references to section numbers are to the Wisconsin Statutes unless otherwise noted.

The following tax releases are included:

Individual Income Taxes

1. Penalty Related to Sale or Distribution of Business Assets or Assets Used in Farming to a Related Person (p. 23)
2. Thrift Savings Plan Distributions (p. 24)
3. Withholding Under an Adoption Assistance Program (p. 24)

Sales and Use Taxes

4. Admissions — County Fairs (p. 25)

INDIVIDUAL INCOME TAXES

1 Penalty Related to Sale or Distribution of Business Assets or Assets Used in Farming to a Related Person

Statutes: Sections 71.05(6)(b)25 and 71.83(1)(d), Wis. Stats. (1997-98)

Background: Section 71.05(6)(b)25, Wis. Stats. (1997-98), provides a subtraction from federal adjusted gross income when computing Wisconsin adjusted gross income for certain gain on the sale or other disposition of business assets or assets used in farming when such assets were sold or disposed of to a related person.

Section 71.83(1)(d), Wis. Stats. (1997-98), provides that if a person who purchases or otherwise receives business assets or assets used in farming, of which the gains realized by the transferor on the sale or disposition of such assets are exempt from taxation under sec. 71.05(6)(b)25, Wis. Stats. (1997-98), sells or otherwise disposes of the assets within two years after the person purchases or receives the assets, the person is subject to a penalty.

The penalty is equal to the amount of income tax that would have been imposed on the capital gains received by the transferor if the subtraction in sec. 71.05(6)(b)25, Wis. Stats. (1997-98), did not apply, multiplied by a fraction. The denominator of the fraction is 24 and the numerator is the difference between 24 and the number of months between the date on which the person purchased or otherwise received the assets and the month in which the person sells or otherwise disposes of the assets.

Question 1: Does the penalty in sec. 71.83(1)(d), Wis. Stats. (1997-98), apply when there has been an involuntary conversion of assets that were purchased or otherwise received