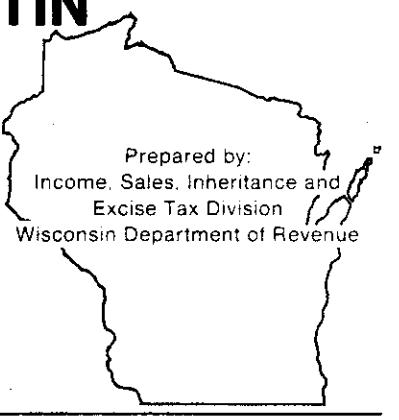
WISCONSIN TAX BULLETIN

Subscriptions available from:

Wisconsin Department of Administration
Document Sales
P.O. Box 7840
Madison, WI 53707
Annual cost - $5.00 (plus sales tax)

April 1986
NUMBER 46



NEW TAX LAWS

The Wisconsin Legislature has enacted changes to the Wisconsin tax laws. Attached to this issue of the Wisconsin Tax Bulletin is a supplement containing brief descriptions of the new laws enacted as of March 15. Any laws enacted after this date will be reported in the July Bulletin.

COUNTY SALES TAX BEGINS APRIL 1, 1986 IN BARRON AND DUNN COUNTIES

On April 1, 1986, the ½% county sales and use tax began for Barron and Dunn Counties. The *Tax Report* included with the January 1986 *Wisconsin Tax Bulletin* (page 21) explains how this new county tax applies to retailers and other persons.

On page 38 of this bulletin is a copy of the March 1986 *Tax Report* which was sent in late March to all retailers who have a seller's permit. A copy of the revised sales and use tax return (Form ST-12) is shown on page 2 of this March *Tax Report.*

Note: Brown County will not have a county tax. Although the December 1985 *Tax Report* indicated Brown County would have a county tax beginning April 1, 1986, the Brown County Board in February 1986 adopted an ordinance to repeal the tax.

SALES FACTOR CHANGED FOR MULTI-STATE CORPORATIONS

The May 9, 1985 Wisconsin Tax Appeals Commission decisions in *United States Steel Corporation vs. Wisconsin Department of Revenue* and *International Business Machines Corporation vs. Wisconsin Department of Revenue* altered the Wisconsin sales factor computation under s. 71.07 (2) (c), 1983 Wis. Stats., and Wis. Adm. Code Section Tax 2.39 (5).

IN THIS ISSUE

However, in February 1986, a new law, 1985 Wisconsin Act 120, was enacted. This new law reversed in part the effect these decisions had on the sales factor computation. On page 22 of this bulletin is a Tax Release which reviews the *U.S. Steel* and *IBM* decisions by the Wisconsin Tax Appeals Commission as they are related to the sales factor issue. The Tax Release also explains the effects of 1985 Wisconsin Act 120 on the sales factor computation, including the option to apply this new law to tax years prior to the 1986 taxable year.

REFUND QUESTIONS

Do you have a question about your income tax or homestead credit refund check? First, wait at least 10 weeks after filing your Form 1, Form 1A or Schedule H. Then, call or write to: Wisconsin Department of Revenue, P.O. Box 8903, Madison, Wisconsin 53708, (608) 266-8100.

In your inquiry be sure to include your name and social security number, the name and social security number of your spouse if you are married, your address, the approximate date you filed your return, and your phone number where you can be reached during the day.

NEW PROPERTY TAX DEFERRAL LOAN PROGRAM

The State of Wisconsin has a new program to loan money to individuals who are age 65 or older to help them pay the property taxes on their homes. Persons age 65 or older with total household incomes for 1985 of $20,000 or less might qualify for a loan to pay their 1985 property taxes. This new loan program does not replace the Wisconsin Homestead Credit Program. Participants in the new loan program may also file a Homestead Credit Claim.

Applications must be filed by June 30, 1986 for 1985 property taxes payable in 1986. See *Wisconsin Tax Bulletin #45*, January 1986 for more details or contact any Department of Revenue office to request an information brochure about the property tax deferral loan program.

EXTENSIONS TO FILE FOR INDIVIDUALS

Forms 1 and 1A

Any extension of time granted by the Internal Revenue Service for filing federal returns also extends the time for filing the corresponding Wisconsin individual income tax returns. A copy of the federal extension (Form 4868 for a 4-month extension, or Form 2688 for an additional extension) must be filed with the Wisconsin return. If the Internal Revenue Service for any reason refuses to grant an extension or terminates one previously granted, the Wisconsin income tax return is due on the same date as the federal return.

If you are not applying for a federal extension, but need extra time for a Wisconsin return, a 30-day extension of time to file may be requested on Wisconsin Form I-101, "Application for Extension of Time to File Wisconsin Individual Income Tax Return." The application for extension must be submitted on or before April 15, 1986.

If an individual who has been granted an extension files a return and has a tax due, the amount due is subject to interest at the rate of 12% per year for the extension period (s. 71.10(5)(b), Stats.). To avoid the payment of interest, individuals may pay the tax due on or before the original due date of the return. A Wisconsin "Declaration Voucher", 1985 Form 1-ES, should be submitted with any payment made. This will ensure that the payment is properly credited to the individual's account. Individuals using a federal extension can obtain a 1985 Form 1-ES from any Department of Revenue office. Individuals applying for a Wisconsin extension may use the 1985 Form 1-ES that is attached to the bottom of the application for the Wisconsin extension.

U.S. citizens who are not in the United States or Puerto Rico on April 15, 1986 are allowed an automatic extension until June 16 to file their returns. These persons do not have to request an extension, but should attach a statement to their returns indicating that they were out of the United States and Puerto Rico on April 15.

Applications for extensions and related correspondence should be sent to:

Wisconsin Department of Revenue
P.O. Box 8903
Madison, Wisconsin 53708

Schedules H (Homestead) and FC (Farmland Preservation Credit)

No extensions of time are available for filing claims for the above credits.

1985 Homestead claims must be filed no later than December 31, 1986. Farmland preservation credit claims for 1985 must be filed no later than 12 months after the farmland owner's 1985 taxable year ends (e.g., December 31, 1986 for calendar year taxpayers).

INDIVIDUALS' 1986 ESTIMATED TAX REQUIREMENTS

Estimated income tax payments are tax deposits made during the year to prepay the tax that will be due when the individual's income tax return is filed. If the individual does not make the estimated tax payments when required, a penalty may be assessed.

Every individual, or married couple filing jointly, is required to file a 1986 declaration of Wisconsin estimated tax (Form 1-ES) if the individual or couple expects to have a balance due of $100 or more with their 1986 income tax return.

The due date for individuals and couples required to file a 1986 declaration during the first quarter of 1986 is April 15, 1986. Installment payments are also due on June 16, 1986, September 15, 1986 and January 15, 1987 for calendar year taxpayers.

Nonresidents as well as residents are required to file declarations of estimated tax. A trust or estate is not required to file a declaration for 1986, but must file a declaration for its 1987 taxable year and thereafter (except that a declaration of estimated tax does not have to be filed for the first taxable year of an estate).

CORPORATIONS: 4TH QUARTER ESTIMATES DUE EARLIER

A corporation must make installment payments of estimated tax if it can expect to have a tax liability for the year of over $500. Installment payments for 1986 taxable years are due on the fifteenth day of the third month, sixth month, ninth month and twelfth month of the taxable year (under prior law the 4th quarter installment payment was not due until the fifteenth day of the first month after the close of the taxable year).

If a required installment is not paid by its due date, an addition to the tax may be assessed on the amount of the underpayment for the period of the underpayment. In determining the underpayment for 1986, the percentage of tax that is required to be prepaid is 90% of the net tax liability shown on the return.

Corporations should keep in mind the change in Wisconsin law (1983 Wisconsin Act 27) concerning exceptions 1 and 2 (s. 71.22(10)(a) and (b), Stats.) to avoid the addition to the tax. Beginning with 1984 taxable years, corporations with Wisconsin net income of $250,000 or more are no longer eligible for these exceptions. These exceptions continue to apply to corporations with less than $250,000 of net income.

Corporations' installment payments of estimated tax are reported on Form 4-ES, the Wisconsin Corporation Declaration Voucher. Corporations who received a preprinted Form 4-ES in the mail are urged to file on that form rather than on a facsimile, since the preprinted forms are color coded and are less costly and faster to process.

OFFICE AUDITING: NUMBER AND TYPE OF ADJUSTMENTS MADE

Office auditing plays a crucial role in the Department's responsibility of administering the state's income tax laws. Both the income tax returns of individuals and the franchise/income tax returns of corporations are routinely office audited. Usually a taxpayer's returns covering a three-year period are audited at one time.

An office auditor examines tax returns to verify the correctness and completeness of the information be-

ing reported. For example, income, deductions, exemptions and credit items are reviewed to see that taxes have not been either underpaid or overpaid. When an office auditor requires additional information to complete the review of a return, the information is typically requested from the taxpayer by letter. In some instances the request may be made by telephone.

In the 1984-1985 fiscal year, nearly one million corporation and individual income tax returns were office audited. Such audits resulted in 34,300 assessments of additional tax against individuals and 5,300 against corporations. These assessments amount to about $41 million in additional tax. In addition, this auditing activity generated 18,300 refunds totalling $16.3 million.

Some of the problem items most frequently involved in office audit adjustments include:

- Incorrect amounts of credit claimed for estimated tax payments made.
- Incorrect amounts of itemized deductions are claimed.
- Treatment of capital gain income or loss is incorrectly reported.
- Homestead Credit and Farmland Preservation Credit claims filed in error.
- Incorrect amounts of net operating loss carryover.
- Incorrect amounts of personal exemptions.
- Incorrect computations in part-year and nonresident tax situations.
- Failure to report minimum tax.

NEW BUREAUS CREATED

The Compliance Bureau of the Wisconsin Department of Revenue has been split into two separate bureaus which will be called the Tax Processing Bureau and the Compliance Bureau. The original Compliance Bureau was previously the largest bureau in the Department.

The Tax Processing Bureau will have 130 permanent employes and the equivalent of 93 staff years of limited term employes. The bureau is responsible for processing in excess of 5,000,000 documents, depositing and accounting for revenues collected and storing taxpayer files.

The Compliance Bureau will have 233 permanent employes. The bureau is responsible for registering taxpayers for sales and withholding taxes, obtaining returns from nonfilers, providing taxpayer assistance and collecting delinquent taxes.

Jerome Pionkowski, previous Director of the Compliance Bureau, assumed the responsibilities for managing the Income, Sales, Inheritance and Excise Tax Division on July 22, 1985. Diane Hardt has been named Director of the new Tax Processing Bureau, and Eugene Fitzgerald is the new Director of the Compliance Bureau.

JAIL TERMS FOR CRIMINAL VIOLATIONS OF WISCONSIN STATE INCOME TAX LAWS

A Milwaukee man has been ordered to serve eight months in jail and pay $650 in fines for criminal violations of the Wisconsin state income tax law. Christopher L. Niesl was sentenced in Dane County Circuit Court, Branch 7, by Circuit Judge Moria Krueger after a probation hearing. Judge Krueger ordered Niesl to serve three months in jail and pay a $250 fine on the first count and she ordered him to serve five months in jail and pay a $400 fine on the second count.

Niesl was charged with failing to file state income tax returns on gross income of more than $39,000 for 1980 and $38,000 for 1981. Niesl was convicted on both counts after a jury trial in November, 1983 and ordered to serve probation by Judge Krueger on February 9, 1984. Niesl did not comply with the conditions of probation.

A Madison attorney has been ordered to serve probation, pay $750 in fines and serve thirty days in the Dane County jail for criminal violations of the Wisconsin state income tax law. J. Thomas Haley was placed on two years probation in Dane County Circuit Court, Branch 12. Reserve Judge Frederic P. Kessler withheld sentencing and ordered Haley to serve two years probation to run concurrently on each of two counts of failing to file state income tax returns on time. He was charged with failing to file timely state income tax returns on gross income of more than $31,000 for 1980 and $39,000 for 1981. He was found guilty on both counts after trial by a jury in November, 1985. Under the conditions of probation, Haley must pay a $500 fine on the first count and serve thirty days in jail. He must pay a $250 fine on the second count, pay all taxes due for 1980 and 1981, file future returns on time and contribute 200 hours of volunteer community service.

Failure to file a Wisconsin state income tax return is a crime punishable by a fine of not more than $500 or imprisonment not to exceed six months or both for income tax returns due prior to July 20, 1985. Beginning July 20, 1985, the criminal penalty is a $10,000 fine or imprisonment not to exceed nine months or both. In addition to the criminal penalties, Wisconsin law provides for substantial civil penalties on the civil tax liability. Assessment and collection of the additional taxes, penalties and interest due follows conviction for criminal violations.

GIFT TAX RETURNS DUE APRIL 15

1985 Wisconsin gift tax reports must be filed if the total value of taxable gifts given by one donor (person giving the gift) to one donee (person receiving the gift) exceeds $10,000. Gift tax reports of the donee and donor for 1985 must be filed by April 15, 1986.

The donor reports gifts made on Form 7. On this form the donor enters the description and value of the gifts made to each donee.

The donee reports the gifts he or she received on Form 6, and includes the description and value of the gifts received from one donor. If the donee received gifts from more than one donor during that year, the donee must file a separate report of gifts received from each donor.

The gift tax due is figured on Form 6. In determining the 1985 gift tax due, an annual exemption of $10,000 is allowed for all gifts made during a calendar year by one donor to one donee. Gifts to a spouse are completely exempt from Wisconsin gift tax. A lifetime personal exemption of $25,000 is allowed for gifts to lineal issue (children, grandchildren), lin-

eal ancestors (parents, grandparents), the wife or widow of a son, the husband or widower of a daughter, an adopted or mutually acknowledged child, and a mutually acknowledged parent. There is no lifetime exemption allowed to other donees.

Beginning in 1986 the lifetime exemption for property transferred to lineal issue and lineal ancestors (children, grandchildren, parents, grandparents) etc., will increase to $50,000. Also, for gifts occurring on or after January 1, 1986 the top marginal gift tax rate is reduced from 30% to 20%.

REMINDER! DEPENDENTS WITH UNEARNED INCOME

There is a special filing requirement for dependents with unearned income. Persons who are claimed as a dependent by another taxpayer, and who have unearned income (for example, interest or dividends) of $1,000 or more are required to file a Wisconsin income tax return.

A dependent with unearned income may elect to itemize deductions for 1985 or claim the standard deduction. If the standard deduction is claimed, the amount of deduction is limited to the lesser of the total earned income or the standard deduction. For example, if the dependent had total income of $1,700 consisting of wages of $500 and interest of $1,200, his or her standard deduction is limited to $500.

DO YOU HAVE SUGGESTIONS FOR 1986 TAX FORMS?

For 1986 the individual income tax forms (Forms 1 and 1A) will be redesigned and simplified. Do you have suggestions for helping to simplify these forms and instructions? Do you have suggestions for improving any other Wisconsin tax forms and instructions?

Send your suggestions to the Wisconsin Department of Revenue, Director of Technical Services, P.O. Box 8933, Madison, WI 53708. Please be specific and send your suggestions in early. The Department appreciates hearing from you.

NEW ISI&E DIVISION RULES AND RULE AMENDMENTS IN PROCESS

Listed below, under Parts A and B, are proposed new administrative rules and amendments to existing rules that are currently in the rule adoption process. The rules are shown at their stage in the process as of March 1, 1986. Part C lists new rules and amendments which were adopted in 1986.

("A" means amendment, "NR" means new rule, "R" means repealed and "R&R" means repealed and recreated.)

A. Rules at Legislative Council Rules Clearinghouse

11.03	Elementary and secondary schools-A
11.05	Governmental units-A
11.65	Admissions-A
17.01	Administrative provisions-NR*
17.02	Eligibility-NR*
17.03	Application and review-NR*
17.04	Repayment of loan-NR*

*These rules will be part of a new chapter, Chapter 17, which will contain rules relating to the Wisconsin Property Tax Deferral Loan Program.

B. Rules at Legislative Standing Committees

None

C. Rules Adopted in 1986 (in parentheses is the date the rule became effective)

2.045	Information returns: form 9c for employers of nonresident entertainers, entertainment corporations or athletes-R (1/1/86)
3.22	Real estate and personal property taxes of corporations-R (1/1/86)
3.30	Depreciation and amortization, leasehold improvements: corporations-R 1/1/86)
3.31	Depreciation of personal property of corporations-R (1/1/86)
3.61	Mobile home monthly parking permit fees-R (1/1/86)
11.71	Computer industry-NR (3/1/86)
11.83	Motor vehicles-A (3/1/86)

D. Emergency Rules

Chapter 17, relating to the property tax deferral loan program (2/18/86).

The following sales tax rules to incorporate county sales/use tax provisions will be published and effective in mid-March, 1986:

11.001	Definitions and use of terms-A
11.32	"Gross receipts" and "sales price"-A
11.68	Construction contractors-A
11.83	Motor vehicles-A
11.92	Records and record keeping-A
11.95	Retailer's discount-A
11.97	"Engaged in business" in Wisconsin-A

REPORT ON LITIGATION

This portion of the WTB summarizes recent significant Tax Appeals Commission and Wisconsin court decisions. The last paragraph of each decision indicates whether the case has been appealed to a higher court.

The last paragraph of each WTAC decision in which the department's determination has been reversed will indicate one of the following: (1) "the department appealed," (2) "the department has not appealed but has filed a notice of nonacquiescence" or (3) "the department has not appealed" (in this case the department has acquiesced to Commission's decision).

The following decisions are included:

Individual Income Taxes

John Clifford
Federal income taxes—no effect on state tax

Chris Culver
Splitting of income—husband/wife

Wendy L. LaBadie
Basis of assets

Andre Leveque
Tax sheltered annuity

Robert E. Nash
Contributions, charitable

James O. Werner
Splitting of income—husband/wife

Roy A. Zamecnik
Penalty—fraud

Corporation Franchise/Income Taxes

Allis-Chalmers Corporation
Manufacturer's sales tax credit
Net business loss carryforward
Interest on assessments

All-Power, Inc.
Allocation of income—separate accounting

American Telephone & Telegraph Company
Allocation of income—separate accounting
Unitary business

Cedarburg Mutual Insurance Company
Insurance companies—add-back for taxes

Central Wisconsin Wholesale, Inc.
Bad debts—change in accounting method

Consolidated Freightways Corporation of Delaware
Apportionment—interstate motor carriers

Kohler Co., Kohler Co.- Successor to Kohler International Ltd., KOHLERCO DISC, INC. and KIL DISC, INC.
Domestic International Sales Corporation
Equitable offset
Interest on assessments

NCR Corporation
Deductions—federal income taxes

News/Sports Radio Network, Inc. and Wisconsin Independent Radio Network
Consolidated returns

Star Line Trucking Corporation
Deductions—motor carriers' operating authorities

Sales/Use Taxes

Advance Pipe & Supply Co., Inc. and Milwaukee Sewer Pipe & Supply Co., Inc.
Construction contractors

Frisch, Dudek and Slattery, Ltd.
Retailer—who must register

Montgomery Ward & Co., Inc.
Transportation charges

James M. Salmon d/b/a General Lighting and Maintenance
Services subject to the tax

Senior Golf Association of Wisconsin, Inc.
Admissions

Troyanek's Tap & Line Service, Inc.
Services subject to the tax

Wisconsin State Telephone Association, et al.
Telecommunication services

Wisconsin Telephone Company, et al.
Telecommunication services

INDIVIDUAL INCOME TAXES

John Clifford vs. Wisconsin Department of Revenue (Court of Appeals, District I, October 22, 1985). John Clifford appealed a judgment of the Circuit Court dismissing his petition for judicial review of an adverse decision of the Wisconsin Tax Appeals Commission.

The facts of this case are undisputed. Clifford had made a claim against the Wisconsin Department of Revenue before the Commission, asserting that the amount of federal withholding tax withheld from his income was exempt from Wisconsin state taxes. The Commission issued a decision and order dated January 20, 1984, denying Clifford's claim. Clifford sent a petition for rehearing by certified mail on February 9, 1984. The petition was actually filed on February 10, 1984, the day it was received by the Commission. On March 10, 1984, the Commission issued an order denying Clifford's request for rehearing as untimely filed. Clifford then filed a petition for review with the Clerk of Circuit Court in Milwaukee County on March 30, 1984. The Circuit Court dismissed Clifford's appeal based on lack of subject matter jurisdiction.

The first issue is whether Clifford timely filed his petition for rehearing with the Commission as required by s. 227.12(1), Wis. Stats. The statute expressly required filing with the Commission within twenty days, not mailing within twenty days. The twenty day period in which Clifford could have filed his petition for rehearing expired on February 9, 1984. Because Clifford's petition for rehearing was not received by the Commission until the twenty-first day, it was not timely filed.

The second issue is whether Clifford timely filed his petition for review with the Circuit Court. Section 227.16, Wis. Stats., requires that the petition for rehearing be "requested under s. 227.12." Section 227.12 clearly specifies that the petition for rehearing must be filed within twenty days. Since Clifford's petition for rehearing was not timely filed, rehearing was not properly "requested under s. 227.12." Clifford was therefore required to file his petition for Circuit Court review within thirty days of the service of the Commission's original adverse decision. That decision was issued January 20, 1984. Thus, to be timely, Clifford would have had to file his petition for review with the Clerk of the Circuit Court by February 19, 1984. He did not and, therefore, lost his right to do so.

Because Clifford did not timely file his petition for rehearing with the Commission, his petition for review with the Circuit Court was also untimely filed. The Circuit Court, therefore, had no subject matter jurisdiction over his petition for review. Thus, the Court of Appeals affirmed the Circuit Court's judgment dismissing the petition.

The taxpayer has appealed this decision to the Supreme Court. On February 18, 1986, the Supreme Court denied his petition for review.

Chris Culver vs. Wisconsin Tax Appeals Commission, Department of Revenue (Circuit Court of Chippewa County, November 11, 1985). This is an appeal of a decision and order of the Wisconsin Tax Appeals Commission affirming the Wisconsin Department of Revenue's denial of the taxpayer's petition for redetermination of an assessment of additional income taxes for the year 1979. The sole issue presented by this appeal is whether or not the taxpayer may properly deduct certain sums of money paid his wife and claimed as expenses on his 1979 income tax return. (See WTB #44 for a summary of the Wisconsin Tax Appeals Commission's decision.)

Under a written agreement entered into on December 31, 1978 and effective throughout the entire year of 1979, the taxpayer contracted to pay his wife, Linda, $6,000 yearly for bookkeeping services plus $6 per hour for farm work not related to bookkeeping, as well as an incentive payment of 25% of the net farm profit.

No payroll checks were issued to Linda; she was compensated for work in the following manner. The taxpayer received checks from the brothers' joint checking account

representing his net share of the farm receipts. The taxpayer's wife endorsed these checks in his name and deposited them, less cash withdrawals in many instances, into the joint checking account maintained by her and the taxpayer. The taxpayer signed statements throughout the year which signified that the deposits to this joint checking account were considered to be compensation to Linda as compensation under the agreement of December 31, 1978. Although the taxpayer's wife claimed to be free to use the checking account as she saw fit, she was responsible for most of the family's personal living expenses, and funds in the account were expended for the benefit of the taxpayer and his family.

Though the Commission did find that an employment contract had been entered into on December 31, 1978, that the wife did bookkeeping work and performed farm chores, and that payments were made to the wife pursuant to that contract, it did not find such payments to be a reasonable amount for services actually rendered. The Commission concluded that no bona fide employer-employe relationship existed and that the sums paid to the wife were not deductible wages.

The Circuit Court felt there is substantial evidence in the record to support the conclusions reached by the Commission. Therefore, the Circuit Court affirmed the decision and order of the Commission.

The taxpayer has appealed this decision to the Court of Appeals.

Wendy L. LaBadie vs. Wisconsin Department of Revenue (Circuit Court of Milwaukee County, November 19, 1985). The taxpayer sought reversal of a decision and order by the Wisconsin Tax Appeals Commission which affirmed the department's denial of her claim for refund for 1981.

The department originally disallowed the taxpayer's claim for a refund in part because it concluded that gain incurred from the appreciation of a constant basis asset during a period of nonresidence may not be excluded from Wisconsin taxable income if the assets were acquired while the taxpayer was a resident of Wisconsin. The Wisconsin Tax Appeals Commission also concluded that a Wisconsin taxpayer who purchased and sold corporate stock while a resident of Wisconsin cannot exclude from the computation of taxable gain realized from the sale, appreciation on the stock which occurred during a period of nonresidence. (See WTB #42 for a summary of the Wisconsin Tax Appeals Commission's decision.)

The taxpayer was a resident of Wisconsin until December 31, 1977. From January 1, 1978 until September 1, 1980, she was not a resident of Wisconsin. On September 1, 1980, she reestablished her Wisconsin residence. There are three particular periods of time involved in this case in which stock was transferred to the taxpayer by gift.

A. Prior to January 1, 1965, the taxpayer acquired 58,936 shares of stock. The aggregate fair market values of these shares on the various dates she received them totaled $62,894.32. The aggregate fair market value of these shares on December 31, 1977 was $360,983; and on September 1, 1980, it was $1,312,246.85.

B. From January 1, 1965 through December 31, 1977, the taxpayer acquired 7,408 shares of stock. The aggregate fair market value of these shares on December 31, 1977 was $45,374; and on September 1, 1980, it was $164,943.75.

C. From January 1, 1978 through August 31, 1980, the taxpayer acquired 1,054 shares of stock. The aggregate fair market value of these shares on September 1, 1980 was $23,467.97.

The total number of shares of stock owned by the taxpayer on and after September 1, 1980 was 67,398. They were all sold on September 18, 1981 on an installment basis with 5% of the purchase price paid in 1981 and the balance thereafter. The taxpayer based her Wisconsin basis for the shares on her federal adjusted basis in order to determine the amount of 1981 Wisconsin taxable capital gain.

The taxpayer filed an amended Wisconsin income tax return on January 14, 1983, claiming a refund of $5,762.15 in Wisconsin income tax due to Wisconsin basis adjustments. The adjustments which were disallowed were obtained by deducting the appreciation values of the stock for the period of nonresidence. Thus, the Wisconsin basis adjustments were modified to reflect no appreciation in value of the stock for the period January 1, 1978 to September 1, 1980. The taxpayer argued that because she was a nonresident during that period of time, the appreciation of the value of the stock during those years cannot be used in computing the gain realized upon the sale of such stock. She based her argument on former Wis. Adm. Code section Tax 2.97, which applied to all sales prior to August 1, 1982.

The department allowed a portion of the taxpayer's claim for refund as it pertained to the 1,054 shares of stock acquired by her during her period of nonresidence. The reason for this allowance was because the taxpayer did acquire those shares prior to becoming a resident again on September 1, 1980. The department denied the remainder of the taxpayer's claim because those shares were acquired at a time when she was a Wisconsin resident. The taxpayer asserted that since she acquired the bulk of stock prior to becoming a resident on September 1, 1980, section Tax 2.97 should apply to exclude the value of appreciation of the 66,344 shares for the nonresidence period in determining taxable income.

The Circuit Court concluded that the department correctly disallowed the taxpayer's claim. A proper interpretation of the rule requires one to have acquired the stock during a period of nonresidence as opposed to a period of residence in order for it to be applicable.

The taxpayer has appealed this decision to the Court of Appeals.

Wisconsin Department of Revenue vs. Andre Leveque (Circuit Court of Dane County, January 7, 1986). This matter is before the Circuit Court for review of a decision of the Wisconsin Tax Appeals Commission which found that certain annuity payments received by Andre Leveque from the State Teachers Retirement System were exempt from Wisconsin income tax under s. 71.03(2)(d), Wis. Stats.

The facts in this case are not disputed. Andre Leveque was a member of the faculty at the University of Wisconsin from 1930 until he retired in 1970. When he retired he began receiving payments from the Department of Employe Trust Funds, part of which were identified by the Fund as "regular annuity" payments and part of which were identified as "tax deferred additional annuity" payments.

The issue before the Circuit Court is whether the latter payments are excluded from gross income under s. 71.03(2)(d), Wis. Stats.

There is no dispute over the fact that Andre Leveque was a member of the state teachers retirement system as of December 31, 1963 and that the payments he received came from the system. However, part of the payments came as a result of his mandatory participation in a retirement fund while the payments labeled "tax deferred additional annuity" payments came as a result of voluntary payments which Mr. Leveque began making in March of 1964. The department claimed that the Legislature did not intend to exclude the payments resulting from voluntary contributions from gross income. The department relied on the comments of the legislative advisory committee which accompanied s. 71.03(2)(d) when it was drafted in 1963.

The intent of the Legislature in adopting s. 71.03(2)(d), Wis. Stats., was to remove a tax inequity while not penalizing those who already held the exemption. There is no doubt that at the time s. 71.03(2)(d) was adopted, Mr. Leveque had not begun making voluntary payments. It would be absurd to interpret a statute that was clearly intended to limit tax exemptions as allowing Leveque to expand his exemption. This fact combined with the obvious inequity of allowing the taxpayer to completely escape taxation on this income leaves room for no choice but to conclude that the voluntary annuity payments received by Mr. Leveque were not exempted from Wisconsin income tax.

In other words, it makes good sense to permit a professor, civil servant or judge to defer the payment of income tax on a portion of his or her income until after retirement when presumably his or her tax rate will be lower and income less; however, completely exempting such income is another matter. The reasoning of the Commission was both illogical, unfair to other taxpayers and clearly not intended by the Legislature.

Therefore, pursuant to s. 227.20(5), Wis. Stats., the decision of the Wisconsin Tax Appeals Commission is hereby set aside. The original determination of tax liability by the department shall be reinstated.

The taxpayer has not appealed this decision.

Robert E. Nash vs. Wisconsin Department of Revenue (Wisconsin Tax Appeals Commission, November 29, 1985). The issue before the Commission was whether or not the taxpayer can deduct the amount of $13,108.20 or a part thereof as a Section 170 deduction as a charitable contribution, or in the alternative, as a Section 162 ordinary and necessary business expense.

Robert E. Nash is a full time physician employed at St. Francis Hospital in Milwaukee, Wisconsin and is not intending to become a minister (auditor) in his religion. He is a member of the Church of Scientology and has been a member for about fifteen years. This church is an organization contributions to which are deductible pursuant to Section 170 of the Internal Revenue Code.

During 1982, the taxpayer wrote four checks to the Church of Scientology in the amounts of $1,210, $565, $4,725 and $6,608.20, for a total of $13,108.20. All of the amounts given to the church were for a church process called "auditing" except the check for $565 which was for training routines which were described as part auditory and part general courses.

Auditing is a process by which the church member and "auditor" (minister) participate in pastoral counseling and development of the member's spirituality. Counseling is received on stress, organization of daily routine and communications in addition to spirituality. The auditing is offered as a package and has a set fee for participation. A discount is offered for early payment by the member.

All payments made by the member are kept in account and after participation in the auditing courses, the member's account is debited. If, after paying the set fee for auditing, the member chooses not to take the course, the member may apply for a refund.

The taxpayer took auditing attributed to the check written for $1,210. He did not take any other auditing in the year 1982 although he can apply his account to future auditing.

The Commission held that payments made by the taxpayer to the Church of Scientology were made to purchase services primarily from the incentive of an anticipated benefit and not as a gift and as such do not qualify as a Section 170 Internal Revenue Code deduction. The payments made by the taxpayer to the Church of Scientology do not qualify as educational expenses undertaken for the purpose of maintaining or improving skills required of a practicing physician nor are they a condition to the retention of salary or status in employment.

The taxpayer has not appealed this decision.

James O. Werner vs. Wisconsin Department of Revenue (Wisconsin Tax Appeals Commission, November 1, 1985). The sole issue for determination was whether loss realized by the taxpayer on rental of two residential properties owned by the taxpayer and his wife in equal proportions is limited to one-half the total loss.

The department adjusted the taxpayer's total taxable income for the years under review (1981 through 1983) and only allowed the taxpayer to claim one-half of the total rental losses. The department allocated the remaining one-half of the losses to the taxpayer's wife and joint tenant.

The rental properties which consist of two 6 unit and 4 unit apartment buildings are owned in joint tenancy by the taxpayer and his wife. The taxpayer did most of the repairs and management of the buildings. His wife did some record keeping and bill paying. The taxpayer argued that the income was a result of his management skills and not solely derived from the collection of rent.

The Commission concluded that income or loss arising from the rental of real estate follows the legal title of real estate. Therefore, the department's action on the taxpayer's petition for redetermination is affirmed.

The taxpayer has not appealed this decision.

Roy A. Zamecnik vs. Wisconsin Department of Revenue (Wisconsin Tax Appeals Commission, November 1, 1985). The sole issue for the Commission to determine was whether the Wisconsin Department of Revenue properly applied the 50% pen-

alty (sometimes referred to as the fraud penalty) provided for in s. 71.11(6)(b), Wis. Stats., to the taxpayer's 1980, 1981 and 1982 income tax liability.

During all of the period involved, the taxpayer was employed on a full time basis by United Parcel Service, Inc. of St. Charles, Illinois. He derived $27,712.35 of income in 1980, $32,083.83 in 1981, and $32,663.91 in 1982. Up until 1979, the taxpayer filed his annual Wisconsin income tax return and paid the tax due on a timely basis. The taxpayer did not file a timely Wisconsin income tax return for the 1979 calendar year.

On February 2, 1981, the department issued a notice of estimated 1979 income taxes due against the taxpayer. The taxpayer appealed this action to the Commission alleging that the department's action was contrary to provisions of both the United States Constitution and the Wisconsin Constitution and that he did "not have any sort of income but in fact received only QUID PRO QUO or renumeration in the form of 'wages.' "

On December 16, 1982, the Commission dismissed this appeal on the grounds that the taxpayer's arguments were frivolous and devoid of merit. This decision was affirmed by the Rock County Circuit Court on October 28, 1983.

During the period beginning May 4, 1979 and ending April 27, 1983, the taxpayer executed and filed with his employer a series of Employe's Withholding Allowance Certificates, Forms W-4, claiming he was exempt from Wisconsin income taxes. The taxpayer was not entitled to the exemption allowance he claimed and the certificates were voided by the department on May 19, 1982.

Despite repeated requests from the department, the taxpayer failed to file timely Wisconsin income tax returns and pay the taxes due for the years 1980, 1981 and 1982.

Under date of April 29, 1983, the department requested that the Wisconsin Department of Justice institute a mandamus action against the taxpayer pursuant to the provisions of s. 71.11(30), Wis. Stats. This action was instituted by the Wisconsin Department of Justice in the Circuit Court for Rock County, Wisconsin. On October 19, 1983, the Circuit Court for Rock County issued a judgment ordering the taxpayer to file complete and proper 1980 and 1981 Wisconsin income tax returns within 30 days.

The taxpayer filed his 1980 and 1981 Wisconsin income tax returns with the department on November 28, 1983. He filed his 1982 Wisconsin income tax return with the department on January 18, 1984.

Under date of March 5, 1984, the department issued an assessment against the taxpayer in which it imposed the 50% fraud penalty provided for in s. 71.11(6)(b), Wis. Stats., for each of the years 1980, 1981 and 1982.

The Commission concluded that the department met its burden of proof to establish by clear and convincing evidence that the taxpayer's failure to file timely Wisconsin income tax returns for 1980, 1981 and 1982 was with the intent to defeat or evade the income tax assessment required of him by law. Under the provisions of s. 71.11(6)(b), Wis. Stats., the department's action was proper in assessing the 50% penalty provided.

The taxpayer has not appealed this decision.

CORPORATION FRANCHISE/INCOME TAXES

Allis-Chalmers Corporation vs. Wisconsin Department of Revenue (Wisconsin Tax Appeals Commission, November 14, 1985). The issues in this case are as follows:

A. Manufacturer's sales tax credit—West Allis, Wisconsin plant. The department disallowed claimed manufacturing sales and use tax credits for sales taxes paid on purchases of #4 fuel oil and SG-6 gas (steam generation) during the years 1973 through 1976.

The disallowance of the sales and use tax credit was explained as follows: "To adjust the sales tax credit for . . . oil . . ., and natural gas at division 036 for all years for nonmanufacturing usage based on data submitted by the taxpayer's divisional personnel." During the years 1973 through 1976, all of the #4 fuel oil and SG-6 gas was consumed by the taxpayer in its production of steam which was used by the taxpayer in its manufacturing process. The exhaust steam created by the manufacturing process was either vented in the atmosphere or recycled for use in its hot water heating system.

B. Net business loss. The department disallowed the deduction for the net business loss offsets from 1970 in the amount of $8,717,065. According to the taxpayer's interpretation of the laws of the State of Wisconsin as applied to the net business loss incurred by the taxpayer for the years 1970 through 1972, the taxpayer is entitled to a deduction for a net business loss offset of $761,497 for the tax year 1976. According to the department's interpretation of the laws of the State of Wisconsin as applied to the net business losses incurred by the taxpayer for the years 1970 through 1972, the taxpayer is not entitled to a deduction for a net business loss offset in the tax year 1976.

C. Interest rate. On October 8, 1979, the department commenced its field audit of the taxpayer's franchise tax returns for the years 1970 through 1976. On December 5, 1980, the department sent the taxpayer a letter indicating the estimated additional Wisconsin franchise tax liability for the years 1970 through 1976. On March 30, 1981, the department and the taxpayer held a final conference to discuss the field audit results. On August 1, 1981, the rate of interest charged by the department assessing taxes was increased from 9% to 12% by Chapter 20, Laws of 1981. The department issued a notice of franchise tax assessment dated August 25, 1981, assessing tax and interest for 1976. The interest was computed at the rate of 12% from original due date of the 1976 return (March 15, 1977).

The Commission held as follows:

A. The #4 fuel oil and SG-6 gas was consumed directly in the manufacturing process. Boilers in this process are directly used as machinery and equipment in the step-by-step manufacturing process and therefore all sales tax paid is deductible.

B. The taxpayer is not entitled to apply a 1970 Wisconsin net business loss in calculating its Wisconsin net business loss carryforward to 1976 under s. 71.06, Wis. Stats., as amended by Chapter 224, Laws of 1975.

C. Although the Commission has ruled on the retroactivity of the 12% interest statute, the taxpayer's claim of unconstitutionality of the applica-

tion of the 12% interest rate to this assessment is beyond the Commission's jurisdiction to decide.

Neither the taxpayer nor the department has appealed this decision.

All-Power, Inc. vs. Wisconsin Department of Revenue (Wisconsin Tax Appeals Commission, November 1, 1985). This was a timely filed appeal objecting to the department changing the taxpayer's method of reporting its Wisconsin income for taxation from separate accounting to apportionment and the assessment of additional income taxes resulting therefrom for the period October 1, 1975 through September 30, 1979. The sole issue for the Commission to determine was whether, during the period involved, the taxpayer's business activities in Wisconsin were an integral part of a multistate unitary business within the meaning of s. 71.07(2), Wis. Stats., with its income thus subject to apportionment.

All-Power, Inc. is a corporation engaged in the business of distributing truck parts with its main office or principal place of business located at 3435 South Racine Avenue, in Chicago, Illinois. In addition to its main office in Chicago, the taxpayer also has facilities located in Decatur, Illinois and Butler, Wisconsin.

The taxpayer's facility at Butler, Wisconsin, known as Drive Shaft Clutch and Gear Division, is staffed by one store manager and eight employes which include three salesmen and five counter and shop employes who repair truck and driveshafts. The taxpayer has no corporate officers located in the State of Wisconsin.

Virtually all activities of the taxpayer's Wisconsin operation are directed or controlled by its Chicago headquarters, including accounting, advertising, hiring and firing, inventory control, markup or profit margin, expense account approval, selection of items to be sold, and credit approval.

Except for a small petty cash fund, all monies received by the taxpayer's Wisconsin operation are forwarded to its Chicago headquarters.

The Commission held that the taxpayer's Wisconsin operation, known as Drive Shaft Clutch and Gear Division, is not a discrete business enterprise, but rather is an integral part of the taxpayer's multistate unitary business. The department acted properly in changing the taxpayer's method of reporting its Wisconsin income for taxation from separate accounting to apportionment.

The taxpayer has not appealed this decision.

American Telephone & Telegraph Company vs. Wisconsin Department of Revenue (Wisconsin Tax Appeals Commission, October 31, 1985). American Telephone & Telegraph Company timely filed its Wisconsin income tax returns for its tax years ending December 31, 1972 through 1976 inclusive. On December 14, 1978, the department issued a Notice of Assessment of Additional Tax for the taxpayer's tax years ending December 31, 1972 through 1976 inclusive. The total amount of the deficiency assessed, including tax and interest computed to February 15, 1979, is $3,597,288.90.

American Telephone & Telegraph Company is a New York corporation with its principal office located in New York City, New York. It is a regulated public utility which furnished interstate and international (referred to as "interstate") telecommunications services and is the parent corporation of 21 operating telecommunications companies (known as Associated Companies), Western Electric Company, Incorporated (Western)—a manufacturer and supplier of telecommunications equipment—and Bell Telephone Laboratories, Incorporated—a research and development company. The taxpayer, together with these subsidiaries and two operating telecommunications companies (Associated Companies) in which the taxpayer holds a minority interest, are known as the Bell System.

Each of the 23 Associated Companies furnishes local exchange, wide area and message toll intrastate telecommunications services in its operating territory within each state and participates within this territory jointly with the taxpayer and other non-Bell System telecommunications companies in the furnishing of interstate telecommunications services. Each is a separate corporate enterprise with its own Board of Directors and its own officers. A majority of the members of each company's Board of Directors is composed of persons in the fields of business and finance who are knowledgeable as to local conditions in the operating territory of the company of whose Board they serve. Only one of the members of each of these Boards is an officer of the taxpayer, and none is a director of the taxpayer. These companies are subject to regulation by state and federal regulatory agencies. As of December 31, 1976, these 23 companies collectively employed over 735,000 employes and had investment in telecommunications plant totalling almost 89 billion dollars. The taxpayer has only a minority ownership in two of these companies. The remaining 21 are either wholly owned (16, including the Wisconsin Telephone Company) or more than 85% owned by the taxpayer. Wisconsin Telephone Company has property and employes within the state, and files its own separate Wisconsin income and gross revenues tax returns.

Bell Labs, owned half by the taxpayer and half by Western, conducts scientific research, development and design work in all aspects of the telecommunications business. Funded for this purpose by the taxpayer, Western and the Associated Companies, Bell Labs is a separate corporation with its own Board of Directors and officers. That portion of the expenses of Bell Labs funded by the taxpayer and the Associated Companies is subject to continuous regulatory scrutiny.

Western is a manufacturing corporation with its own Board of Directors and officers, doing business in all 50 states. It is principally engaged in the business of manufacturing and supplying communications equipment and products to the Associated Companies and the taxpayer, and the provision of related engineering and installation services. This work is done pursuant to standard supply contracts between it and its customers. Under these contracts, Western is obligated to meet the equipment needs of the Bell System operating units.

Western's prices and profits are continuously reviewed by the National Association of Regulatory Utility Commissioners (NARUC) - Federal Communications Commission (FCC) Staff Subcommittee on Manufacturing and Service Affiliates with the objective that any savings to Western or a Bell System operating unit which

could arise from its being a part of the Bell System are ultimately passed on to the subscribers. It conducts business in Wisconsin and has property and employes within the state with respect to which it files its own separate Wisconsin income tax returns. As shown by such filed Wisconsin returns, Western conducts approximately 1% of its total business in the state.

The taxpayer is responsible alone or jointly with the other Bell System and non-Bell System telecommunications companies for the construction, ownership, operation and maintenance of a network of interstate telecommunications facilities to provide for interconnection of the Associated Companies and other telecommunication companies in the United States and telephone systems in most other countries throughout the world. Some of these facilities extend into and through the State of Wisconsin, or originate or terminate in Wisconsin. In performing this business, the taxpayer operates, and thus has property or employes or both, in 49 states, including Wisconsin.

As of December 31, 1976, the taxpayer's activities in Wisconsin consisted of the operation and maintenance of the interstate telecommunications system, including a portion of two interstate cable routes (one terminating at Watertown Junction and the other terminating at Stevens Point) and several radio relay routes crossing the state. The property owned and used in Wisconsin in the operation of its interstate business consisted of land, buildings, central office equipment, cable, furniture and office equipment, motor vehicles and materials and supplies. This property had a gross book cost of approximately 99 million dollars, which was about 1.5% of the total gross book cost of property owned and used by the taxpayer in its interstate business operations (approximately 6.8 billion dollars). Approximately 80% of this property in Wisconsin was central office equipment (for purposes of switching, signaling or carrying interstate communications) in eleven central offices in seven Wisconsin cities. The taxpayer also maintained an administrative office in Madison and a District sales office in Milwaukee. It employed at that time 235 employes within the state, 218 of them involved in the operation, control or maintenance of the interstate communications system and 17 involved in the sales of interstate communications services throughout Wisconsin. While the details may have varied from time to time, at all material times prior thereto its property and activities in Wisconsin were substantially the same or similar.

The taxpayer is responsible for (a) the provision to all of the Associated Companies pursuant to license contract agreements of technical assistance, advice and research in all aspects of the communications business, for which it receives fees, the payments of which by the licensees are subject to scrutiny by the various state and federal regulatory commissions; and (b) the investments in its subsidiaries (approximately 29 billion dollars, as of December 31, 1976), which includes the custody and control of securities, receiving dividends, and providing capital to these subsidiaries through either the purchase of additional stock or the making of cash advances. Advances are extended at the prevailing interest rate and repaid to the taxpayer in cash or additional stock. The dividends, interest and license contract fees received by the taxpayer are managed and directed by it in New York, and constitute the taxpayer's principal sources of income other than the income generated by it in connection with the interstate telecommunications business.

The taxpayer files schedules of rates and charges with the FCC with respect to interstate telecommunications services, which schedules are concurred in by other Bell System and non-Bell System carriers who join in the furnishing of such services. In furtherance of its mission (a) to create and maintain a rapid, efficient communications network; (b) to ensure that adequate facilities are provided for the network; and (c) to require the provision of service pursuant to tariffs which offer just and reasonable rates, practices, procedures and regulations, the FCC has been given authority under The Communications Act of 1934 to determine proper rates and promulgate rules affecting interstate services and facilities and has exclusive jurisdiction over the interstate activities and property of all telecommunications carriers, including the taxpayer, the Associated Companies and the over 1,700 other telecommunications companies. All charges for interstate services must be submitted to the FCC for approval and permission must be obtained from the FCC before undertaking any new construction, acquisition or operation of interstate facilities or the introduction, discontinuance or reduction of interstate telecommunications services.

The taxpayer provides only interstate telecommunications services pursuant to interstate tariffs and is regulated by the FCC. The Associated Companies furnish both intrastate and interstate telecommunications services and are subject both to state regulatory authorities (e.g., Wisconsin Telephone Company is regulated by the Wisconsin Public Service Commission) with respect to intrastate services, and the FCC with respect to services they provide within each of their specific operating territories in connection with the interstate communications systems. It is required that separate regulatory policies be administered by separate regulatory authorities. Whereas the FCC has jurisdiction over only interstate services, each state regulatory authority is authorized to regulate only the intrastate services of carriers within its jurisdiction. The degree of control over intrastate telecommunications services within that jurisdiction is similar to that exercised by the FCC over interstate telecommunications services. All charges for intrastate services must be submitted to the appropriate state regulatory authority for approval and permission must be obtained before a carrier may undertake any new construction, acquisition or operation of intrastate telecommunications facilities or introduce, discontinue or reduce intrastate telecommunications services.

The taxpayer receives revenues from its interstate business activities based upon a fair rate of return as determined by the FCC. Each of the Associated Companies and other telecommunications companies receives revenues from its intrastate business activities based upon a fair rate of return as determined by the appropriate state regulatory authority, and revenues from its interstate business activities based upon a fair rate of return as determined by the FCC. A fair rate of return is that which permits a carrier to earn only that amount of income sufficient to meet the demands for telecommuni-

cations services in its operating territory at a reasonable cost to the public, to compensate investors fairly and to continue to attract capital on reasonable terms.

It is necessary for each telecommunications carrier, except the taxpayer, to determine the proportion of its expenses incurred in, and of its plant devoted to, the furnishing of interstate as distinguished from intrastate services. This is done in accordance with the methods set forth in the Separations Manual developed by NARUC and the FCC. These procedures were prescribed by an FCC order and have become part of its rules and regulations. They have been accepted for use by state regulatory bodies. Based upon these procedures, approximately 75-80% of an Associated Company's property and activities is related to the provision of intrastate telecommunications services.

Charges for interstate telecommunications services are in most instances billed to customers by the local carrier and each carrier accounts for this revenue to the taxpayer. These revenues are then divided among all the participating carriers under what is known as the Division of Revenues and Settlements process. In accordance with this process, non-Bell System carriers are first compensated for their participation in furnishing interstate services. Then each of the Associated Companies is reimbursed for its respective expenses attributable to furnishing interstate services determined in accordance with the Separations Manual and the taxpayer is reimbursed for its expenses. The residue is then divided amongst the Associated Companies and the taxpayer to provide a uniform rate of return on the relative value of their net plant investment devoted to the furnishing of interstate services—determined pursuant to the Separations Manual for the Associated Companies. During the period involved, approximately three-quarters of these net interstate revenues went to the Associated Companies and approximately one-quarter went to the taxpayer.

To determine what portion of the interstate revenues received by the taxpayer is attributable to Wisconsin, it utilizes a "50-state study" under which such revenues are divided among the states subject to procedures similar to those used in the Division of Revenues process. During the years in question the Wisconsin percentage was between 1% to 1.5%.

In the years 1975 and 1976, the taxpayer received dividend income from its subsidiaries and nonsubsidiaries of $2,605,840,385 and $2,871,718,743, respectively, as accounted for in its books. These dividends were included by the department in the taxpayer's gross income for the purpose of computing the taxpayer's apportionable income as the department considered to be required by s. 71.07(1m), Wis. Stats.

The dividends from one of the taxpayer's subsidiaries, Wisconsin Telephone Company, were included in the taxpayer's gross income, since they were included in the "General Department Net Income," but the dividends from Wisconsin Telephone Company were deducted as a deductible dividend in arriving at net income subject to apportionment.

Dividends paid by the taxpayer to its stockholders in 1975 and 1976 were $2,166,360,000 and $2,488,875,000 respectively, as accounted for in its annual report to stockholders in those respective years.

Interest paid by the taxpayer to its debt holders in 1975 and 1976 amounted to $538,791,291 and $543,775,611 respectively, as accounted for in its books.

Attached also to each return filed by the taxpayer was a written statement substantially the same as the following language contained in the 1976 return:

> "The (Petitioner) also derives revenues from sources other than, and separate from, the operations of the long distance communications system and such revenues are separately accounted for. These are dividends, interest, license contract and miscellaneous revenues, which result from its investments, its activities in communications research and its services in rendering technical advice and assistance to its associated telephone companies. None of these separate revenues arises from the property owned or business transacted in Wisconsin."
>
> "For reasons apparent from the above explanation, it is necessary to segregate the entire gross income and deductions of the (Petitioner) into two classes, non-apportionable items unrelated to Wisconsin and apportionable items partly related to Wisconsin, and such a segregation is shown on Schedule No. 1 attached to the return. The items segregated as non-apportionable relate to all activities of the (Petitioner) other than the operation of the long distance communications system and those segregated as apportionable relate to the operation of the long distance communications system, part of which is in Wisconsin."

Following the amendment of s. 71.07(1m), Wis. Stats., in 1975 pertaining to the treatment of certain types of intangible income, including dividends and interest, the department has for 1975 and subsequent tax years included in the taxpayer's apportionable Wisconsin income all dividends and interest received from the taxpayer's subsidiaries and other sources. The department also has included in the taxpayer's apportionable Wisconsin income for the tax years 1972 through 1976, the taxpayer's license contract revenues, rents, capital gains and other miscellaneous income, and for tax years 1973 through 1976, the taxpayer's royalty income.

On March 14, 1980, the taxpayer filed with the department a claim for refund, claiming that federal income taxes paid during 1975 and 1976 are deductible under ss. 71.04(3) and 71.02(1)(c), Wis. Stats. The taxpayer and the department agree and stipulate that the issue raised therein, and any refunds or reductions of tax liability resulting from resolution thereof, shall not be foreclosed by the Wisconsin Tax Appeals Commission's determination on other issues in this proceeding not presented by such claim. Any such deduction in tax liability or refund shall be computed and made by the Wisconsin Department of Revenue if and when such result is warranted by a determination addressing the substantive merits of the issue raised by such claim in some other proceeding before the Commission which has become final under ss. 73.01 or 73.015, Wis. Stats., and such reduction or refund shall be made notwithstanding that a final determination shall theretofore have been or thereafter is made with respect to any

other issues in this proceeding, the determination of the issue regarding deduction of federal income taxes being specifically reserved and governed by such final determination in such other proceeding and subject to such further proceedings thereon as the Commission shall deem appropriate to effect the purposes of this stipulation. The parties further stipulate and agree to seek leave of the Commission to amend the pleadings of this proceeding to conform hereto.

The taxpayer claimed that the above assessment is predicated upon the department for the first time departing from its acceptance of the multiform basis upon which the taxpayer had reported its income for more than fifty years and including within the taxpayer's apportionable base income and related expenses from sources other than and separate from the taxpayer's income and expenses attributable to its interstate telecommunications business within and without Wisconsin. Such inclusion of other income, excluding the taxpayer's dividend and interest income, and related expenses for tax years 1972 through 1974 resulted in a refund situation. The significant deficiency assessed for 1975 and 1976 resulted from the addition of the taxpayer's dividend and interest income to the other income included in its apportionable base without any corresponding inclusion in the prescribed apportionment formula of the underlying economic factors which generated the dividend and interest income.

The department's only basis for taxing the taxpayer arose from the taxpayer's conduct of its interstate telecommunications business activities in Wisconsin. For many years, the department accepted the taxpayer's tax returns which included in the taxpayer's apportionable income base only the taxpayer's income from such interstate activities. Section 71.07(1), Wis. Stats., was amended, effective 1975, and the department contended that the effect of such amendment is to require it to include in the taxpayer's apportionable base for tax years 1975 and 1976 several billion dollars of dividends and interest received from the taxpayer's subsidiaries outside Wisconsin without considering the property or activities which produced such income in the factors of the apportionment formula.

It was the taxpayer's contention that the Wisconsin statute does not require any variance from the method accepted by the department for many years and that the department has imposed an apportionment scheme on the taxpayer that taxes income which is not derived from its business or property in Wisconsin and which does not accurately reflect the business of the taxpayer in Wisconsin.

The department argued that (a) the taxpayer's Wisconsin operations constitute an integral part of a unitary business, subject to statutory apportionment of its corporate income, (b) apportionment of the taxpayer's income under the unitary principle is the proper method of taxation as opposed to the multiform method of reporting, (c) the statutory changes in 1975 compelled the department to treat the taxpayer as a single unitary business, (d) under Wisconsin law the apportionment formula may not include the factors of the taxpayer's subsidiary corporations, contrary to the taxpayer's assertion, (e) the department's assessment is not subject to challenge under the U.S. Constitution, and (f) the Commission should hold that the department has properly applied the governing statutes and rules in this case.

AT&T is functionally divided into two divisions, the Long Lines Department and the General Department. Long Lines is responsible generally for the construction, operation and maintenance of a nationwide system of interstate telecommunications facilities and related equipment which serve to interconnect the facilities of over seventeen hundred operating telecommunications companies in the United States as well as telecommunications systems abroad; and some of these facilities extend into and through the State of Wisconsin. In performing this interstate business, Long Lines operates and thus has property or employes or both, in 49 states, including Wisconsin.

The General Department holds and manages the stock owned in these subsidiaries and two minority-owned Associated Companies and provides capital, advice and assistance to them.

The Wisconsin Telephone Company, a wholly-owned subsidiary of the taxpayer, conducts its business, has property and has employes within the State of Wisconsin. The Wisconsin Telephone Company furnishes primarily intrastate telecommunications services entirely within Wisconsin, subject to regulation by the Wisconsin Public Service Commission and pursuant to tariffs on file therewith. It also participates within Wisconsin jointly with Long Lines and other telecommunications companies in the furnishing of interstate telecommunications services, subject to federal regulation.

During the periods involved, the taxpayer's Wisconsin operations constitute an integral part of a unitary business of which the operation of that portion of the taxpayer's business within the State of Wisconsin was dependent upon the operation of the business outside the state and the operation of that portion of the taxpayer's business within the State of Wisconsin was contributory to the operation of the business outside the state.

The assessment and action made by the department are presumed to be correct and the burden of proof is on the taxpayer to show in what respects the department erred in its determination. The taxpayer and its Bell System businesses were not discrete business enterprises, but rather were integral parts of the taxpayer, Bell System's unitary business during the period at issue, and therefore, the taxpayer failed to meet its burden of proof to show the department's assessment to be incorrect.

The Commission held as follows:

A. During the period at issue, the Bell System constituted a unitary business and the taxpayer's business within Wisconsin was an integral part of such unitary business.

B. During the period at issue, the taxpayer is not entitled to determine its income attributable to Wisconsin by an allocation or separate accounting method (or "multiform method"), and the department acted properly in requiring the taxpayer to utilize the apportionment method of determining its income attributable to Wisconsin, pursuant to s. 71.07(1m), Wis. Stats.

C. The 1975 amendment to s. 71.07(1), Wis. Stats., (creating 71.07(1m), Wis. Stats.), which permitted the department to include certain types of intangible income as Wisconsin apportionable income, does not compel inclusion of all of the tax-

payer's intangible income regardless of derivation in Wisconsin apportionable income. Under the holdings in *ASARCO, Inc. v. Idaho State Tax Commission,* 458 U.S. 307, 102 S.Ct. 3103, 73 L. Ed 2d 787 (1982) and *F. W. Woolworth Co. v. Taxation and Revenue Department of New Mexico,* 458 U.S. 354, 102 S.Ct. 3128, 73 L. Ed. 2d 819 (1982), intangible income earned by the taxpayer may only be subject to apportionment in Wisconsin where there exists a "rational relationship" between such income and the taxpayer's business in Wisconsin—that is where the intangible income is not derived from "discrete business enterprises" that in any business or economic sense have nothing to do with the taxpayer's activities in Wisconsin.

D. During the period at issue, the taxpayer's "General Division" was not a discrete business enterprise but rather was an integral part of the taxpayer's unitary business. Pursuant to s. 71.07(2), Wis. Stats., the taxpayer's income derived from the operations of this division including in part, fees from contract services, royalty income, interest earned in short-term investments, and dividend income, including all of the dividend income other than income from Wisconsin Telephone Company, was includable in its Wisconsin apportionable income.

E. During the period at issue, the taxpayer's 23 subsidiaries (Associated Companies, Western Electric Company, Incorporated and Bell Telephone Laboratories, Incorporated) were not discrete business enterprises but rather were integral parts of the taxpayer's unitary business, and pursuant to ss. 71.07(1m) and 71.07(2), Wis. Stats., dividends received by the taxpayer from these subsidiaries were includable in its Wisconsin apportionable income.

F. Under the authority of s. 71.07(2)(e), Wis. Stats., the department adopted Wis. Adm. Code section Tax 2.50 defining the apportionment formula to be utilized in determining the Wisconsin apportionable income of public utilities. For the period at issue, the department acted properly in applying section Tax 2.50 in determining the taxpayer's business income attributable to Wisconsin, and the prescribed formula adopted in section Tax 2.50 did not result in a substantial distortion of the taxpayer's income attributable to Wisconsin.

G. Income from intangibles includable in the taxpayer's 1975 and 1976 Wisconsin apportionable income, come within the intent and meaning of s. 71.07(2)(c)1, Wis. Stats., as "total sales" includable in the denominator of the sales factor.

H. Except as provided in Conclusions of Law, Paragraph G, above, under Wisconsin law, the taxpayer is not entitled to combine the sales, payroll and property of dividend paying subsidiaries in the denominator of the three factors.

I. The Commission does not have the authority of jurisdiction to rule on the constitutional issues raised by AT&T.

The taxpayer has appealed this decision to the Circuit Court.

Cedarburg Mutual Insurance Company vs. Wisconsin Department of Revenue (Wisconsin Tax Appeals Commission, November 1, 1985). In WTB #45 it was indicated that the department had appealed the Tax Appeals Commission's adverse decision dated November 1, 1985 to the Circuit Court. The department has dropped its appeal.

Central Wisconsin Wholesale, Inc. vs. Wisconsin Department of Revenue (Wisconsin Tax Appeals Commission, January 10, 1986). Central Wisconsin Wholesale, Inc. was incorporated as a Wisconsin corporation in July of 1977. During its first full year of operation (1978), the taxpayer, who was on the accrual method of filing, reported and deducted its bad debts on an estimated reserve basis.

The department in the assessment under review converted the taxpayer's method of deducting its bad debts from the estimated reserve method to a direct write-off method and cited s. 71.04(7), Wis. Stats., as authority. This change resulted in an assessment of additional income taxes covering the years 1979 through 1982, which was issued by the department on March 12, 1984.

The taxpayer conceded that it was incorrect in using the reserve method of deducting its bad debt but alleged that the error has been corrected and the year 1978 was closed to change by the statute of limitations. The department argued that the correction it made constituted a change in the taxpayer's method of accounting and that the assessment involved was timely.

The Commission concluded that the taxpayer incorrectly reported and deducted its bad debts on an estimated reserve basis. The department properly converted the taxpayer's method of deducting its bad debts from the estimated reserve method to a direct write-off method per the clear and unambiguous language contained in s. 71.04(7), Wis. Stats. The department's conversion of the taxpayer's method of deducting its bad debts constituted a change in its method of accounting per the terms of Wis. Adm. Code section Tax 2.16(2). The taxpayer's tax years 1979 through 1982 were open to audit and assessment at the time the department's assessment was issued on March 12, 1984.

The taxpayer has not appealed this decision.

Consolidated Freightways Corporation of Delaware vs. Wisconsin Department of Revenue (Wisconsin Tax Appeals Commission, January 17, 1986). The issue to be decided before the Commission was whether the apportionment formula for the apportionment of the income of interstate motor carriers of property provided for in section Tax 2.47, Wis. Adm. Code, imposes a tax on income derived from business transacted and property located outside of Wisconsin in violation of s. 71.07(2)(e), Wis. Stats.

Consolidated Freightways Corporation of Delaware (CF) is a "general commodity" common carrier operating in interstate commerce. CF serves small and large shippers in small and large communities, transporting manufactured and consumer goods. CF is not typically or principally a transporter of truckload and volume shipments but of small individual shipments. Traditionally, less-than-truckload (LTL) shipments weighing under 10,000 pounds have been considered small shipments.

Successful operation of a general commodity carrier requires consolidation of many small shipments for over-the-road or line-haul movement with the constant objective of minimizing the number of handlings of the shipment and the total miles of operation.

The efficient handling of small shipments requires a national freight distribution system for efficient operation. CF's own operations, through a network of terminals and established routes, are a coordinated and organized system for long-haul movement of interstate general commodity freight.

Over-the-road or line-haul operations are effected through a system of regular routes organized into relay legs on which freight and equipment move through to destination but drivers are reversed to return to their domiciles after each relay leg. CF operates four principal east-west transcontinental mainline relays and a series of north-south mainline relays.

Wisconsin's present apportionment formula is:

Factor 1

$$\frac{\text{Gross Receipts From Carriage of Property First Acquired in Wisconsin}}{\text{Gross Receipts from Carriage of Property Everywhere}}$$

Plus Factor 2

$$\frac{\text{Ton Miles of Carriage in Wisconsin (To, From, and Through)}}{\text{Ton Miles of Carriage Everywhere}}$$

Divided by 2 equals Wisconsin apportionment factor.

The Commission determined that the department's apportionment formula, as contained in section Tax 2.47, and the department's method of taxing the taxpayer's income thereunder was not contrary to law and did not result in the taxation of extra-territorial values. The apportionment formula contained in section Tax 2.47 does not distort that portion of the taxpayer's income properly taxable by the State of Wisconsin. Neither the department nor the Commission has the authority to change the method of taxing the taxpayer's income to a "base line" or any other formula used elsewhere.

The taxpayer has appealed this decision.

Kohler Co., Kohler Co.-Successor to Kohler International Ltd., KOHLERCO DISC, INC. and KIL DISC, INC. vs. Wisconsin Department of Revenue (Wisconsin Tax Appeals Commission, November 22, 1985). The issues in this case are as follows:

A. What is the proper treatment under Chapter 71 of the Wisconsin Statutes of the DISCs' income during the years at issue?

B. For tax years 1975 and 1976, were Kohler Co. and KIL entitled to deduct pursuant to s. 71.04(4)(a), Wis. Stats., dividends received from the DISCs?

C. Is the department entitled to an equitable setoff in the amount of $14,616 plus interest based on a computational error against any refund Kohler Co. might be entitled to for 1976?

D. Does the tax assessed against the Kohler Co. by the assessment notice dated February 22, 1982 bear interest at the rate of 12% or 9% within the meaning of s. 71.09(5)(a), Wis. Stats.?

Kohler Co., a Wisconsin corporation with its principal offices at Kohler, Wisconsin, manufactures plumbing products, small gasoline engines and electric generators, a significant part of which are exported. Kohler Co. is the successor by statutory merger on December 31, 1977 to Kohler International Ltd. (KIL).

KIL was a Wisconsin corporation headquartered at Kohler, Wisconsin and was Kohler Co.'s wholly owned international marketing subsidiary. KIL was a substantive operating company which had its own employes, owned some property consisting principally of office furniture and equipment, and maintained branch sales offices in England and Singapore.

KOHLERCO DISC, INC. and KIL DISC, INC. (the DISCs) are Wisconsin corporations headquartered at Kohler, Wisconsin. KOHLERCO DISC, INC. is the wholly owned subsidiary of Kohler Co. and KIL DISC, INC. was the wholly owned subsidiary of KIL until by statutory merger into Kohler Co., it became the wholly owned subsidiary of Kohler Co. The DISCs were formed in September 1974 solely to avail the parent companies of the benefits of the Domestic International Sales Company provisions of Sections 991 through 997 of the Internal Revenue Code (IRC).

The DISC provisions of the IRC were enacted to encourage export trade by U.S. companies with the main objective to keep jobs in the United States, by allowing domestic corporations to defer federal income tax on a percentage of the export sales.

Although the DISC provisions of the IRC are detailed, the basic concept and structure of the DISC deferral device is quite simple. In order to qualify for the DISC deferral device, a manufacturer cannot itself be a DISC but must be a separate corporation. Through a written franchise agreement the manufacturer agrees to sell its goods which qualify for DISC treatment to a DISC which will resell them to the manufacturer's customers.

By regulation, the commission DISC approach was authorized which eliminates the need for double invoicing from the manufacturer to the DISC to the ultimate customer. Commission DISCs and buy/sell DISCs are treated exactly the same, however, and the income of either type DISC under the inter-company pricing rules of IRC Section 994 will be identical.

A part of the DISC's income is returned to the parent shareholder pursuant to IRC Section 995. Originally this was about half the DISC's income but now it is governed by a more complex formula based on the incremental growth of DISC sales. The balance of the DISC's income is retained by the DISC and, since the DISC is not taxed at the federal level, the taxes on this Accumulated DISC Income (ADI), are deferred indefinitely.

In order to remain qualified, the DISC must invest the ADI in certain "qualified export assets" which support export trade activities. The simplest and most commonly used investment is the purchase of the parent company's accounts receivables from export sales.

Under IRC Section 992, the requirements for a DISC are only that it be incorporated under the laws of any state; that 95% of its gross receipts be "qualified export receipts"; that 95% of its assets at year end be "qualified export assets"; that it have $2,500 of capital; that it elect to be a DISC; and that it have a separate bank account and maintain separate books and records. Treas. Reg. 1.992-1(a) states a corporation meeting the above requirements "is treated as a separate corporation for federal tax purposes and qualifies as a DISC even though such corporation would not be treated (if it were

not a DISC) as a corporate entity for federal income tax purposes."

KOHLERCO DISC, INC. and KIL DISC, INC. were typical commission agent DISCs having only the minimal corporate substance and transactions necessary for Kohler Co. and KIL to obtain the DISC benefit of federal tax deferral and no other transactions. The DISCs were each capitalized by issuance of $2,500 of capital stock. Franchise agreements between the parent corporations and the DISCs were executed on September 27, 1974 and April 25, 1975. The DISCs were incorporated in Wisconsin but had minimal corporate activity consisting of annual unanimous consents electing their officers and directors, who were the same as the principal officers of Kohler Co. and KIL, and an annual unanimous consent declaring a dividend to the parent company.

The DISCs had separate books and records which were maintained by employes of Kohler Co.'s corporate accounting department. These consisted of journals and ledgers reflecting commissions paid by the parents to the DISCs and the immediate return of the monies to the parent companies, generally by simultaneous exchange of checks, either as payment of dividends to the parents or for the purchase of parent export account receivables. The latter device permitted the DISCs to satisfy the requirement that at least 95% of their assets be held in qualified export assets.

The DISCs had separate bank accounts but because all payments to the DISCs were immediately returned to the parent companies, they never had more than nominal balances of $192 and $211 respectively, except momentarily for the time it took the checks that were exchanged to clear.

The DISCs' only other records, its commission computation work papers, were also computed and maintained by employes of Kohler Co.'s corporate accounting department. The DISCs' sales were actually sales of the parent companies which parent company sales personnel identified as qualifying for DISC benefits (i.e., foreign destination sales of U.S. manufactured goods). Parent company sales personnel determined which parent company sales qualified for DISC and gave accountants a list of computer numbers identifying those sales in Kohler Co.'s accounting system. The DISCs' income and its books and records were generated by Kohler Co.'s accounting department pursuant to the intercompany pricing rules of IRC Section 994.

The DISCs, having no employes, had no actual involvement or activity in connection with the sales that gave rise to their income.

As required by Treas. Reg. 1.994-1(e)(3), the commission receivable was paid to the DISCs once annually within sixty days of the close of the DISCs' fiscal years ending January 31. The funds were immediately returned to the parent companies in an exchange of checks either as dividends or to purchase parent company export receivables.

The sum total of these transactions was that the DISCs ended up as the nominal owners of parent export receivables paid for with Accumulated DISC Income (ADI) which had not been subject to federal tax. Since the parent companies took federal tax deductions for the commissions paid to the DISCs, the net effect is that part of the parents' income from export sales has been transferred to and set aside in the DISCs wherein the federal taxes on such income are indefinitely deferred.

The DISCs did not carry on any substantial business activities and did not do anything to earn the income they reported. The earnings which the department contends should be taxed to the DISCs are actually the result of Kohler Co.'s labor and employment of capital and should be taxed as such.

In tax years 1975 and 1976, Kohler Co. and KIL received dividends from the DISCs which Kohler Co. and KIL took as deductions pursuant to s. 71.04(4)(a), Wis. Stats. The department disallowed this deduction to Kohler Co. and KIL in tax years 1975 and 1976.

On December 11, 1981, Kohler Co. notified the department of certain Internal Revenue Service adjustments to its income for 1975 and 1976 which resulted in additional Wisconsin franchise tax of $4,910.40 for 1975 and a refund of $2,514.27 for 1976. While making these adjustments the department discovered a computational error in its earlier assessment which increased Kohler Co.'s 1976 tax liability by $14,616.68 resulting in a net additional assessment against Kohler Co. in 1976 in the total amount of $12,102.40. The taxpayer conceded that there was an error in the taxpayer's favor of $14,616.68 made by the department on its original assessment but argued that the department's February 22, 1982 assessment of this amount was beyond the four year statute of limitations, under s. 71.11(21)(bm), Wis. Stats.

In its assessment against Kohler Co. dated February 22, 1982, the department applied a 12% interest rate to deficiencies assessed for tax years 1975 and 1976.

The Commission's conclusions were as follows:

A. Income is taxable to the one who earns it, and therefore, the income of the DISCs should be allocated to the parent corporations, Kohler Co. and KIL for purposes of determining Wisconsin franchise taxes on that income, in order to clearly reflect the income of these corporations.

B. Kohler Co. and KIL are not entitled for the tax years 1975 and 1976 to deductions under s. 71.04(4)(a), Wis. Stats., for dividends received from the DISCs.

C. The department is entitled to offset the refund of $2,514.27 for 1976 to which the taxpayer would otherwise be entitled by reason of Internal Revenue Service adjustments for that year, by virtue of the discovery by the department of a computational error of $14,616. The department is entitled to an offset only against the amount of refund due for 1976.

D. The department acted properly in applying an interest rate of 12% to the tax assessed in the February 22, 1982 assessment pursuant to s. 71.09(5)(a), Wis. Stats., as amended by Laws of 1981, Chapter 20, Section 1090n, which increased the rate of interest on assessments from 9% to 12%.

The department has appealed this decision to the Circuit Court.

NCR Corporation vs. Department of Revenue (Court of Appeals, District IV, January 10, 1986). NCR Corporation (NCR) appealed from a judgment affirming a Wisconsin Tax Appeals Commission decision denying NCR a deduction on its state corporate franchise tax return for federal income taxes paid for the years 1975,

1976, 1977, 1978 and 1980. NCR contended that the Commission's interpretation of s. 71.04(3), 1975 Wis. Stats., to disallow the deduction was erroneous as a matter of law. NCR further argued that, assuming *arguendo* that federal income taxes paid by Wisconsin corporate franchises continued to be deductible, the Legislature's 1981 effort to retroactively eliminate the deduction by amending s. 71.04(3) was unconstitutional. (See WTB #40 for a summary of the Circuit Court's decision.)

The event giving rise to this case was a 1975 amendment to s. 71.04(3) and (3a), 1973 Wis. Stats. Prior to 1975, corporations required to file Wisconsin franchise tax returns were allowed to deduct federal income taxes paid within the year covered by the income tax return. The amount of the deduction, however, was limited to a sum not to exceed 10% of the corporation's net income for the taxable year.

The 1975 amendment deleted the reference to the deductibility of federal income taxes and repealed the 10% limitation. The Legislature, however, did not repeal or amend s. 71.02(1)(c), 1973 Wis. Stats., which refers to the basis on which federal income taxes were to be deducted, or s. 71.11(8)(b), 1973 Wis. Stats., which incorporates the rules set forth in s. 71.02(1)(c).

In challenging the assessment made by the Department of Revenue, NCR contended that the statutory provisions, when read together, unambiguously allow a full deduction for federal income taxes paid. The Commission, however, ruled that s. 71.04(3), 1975 Wis. Stats., is ambiguous and determined that the Legislature's intent was to eliminate the deduction in its entirety. In addition, the Commission determined that acceptance of the statutory interpretation advanced by NCR would lead to an absurd and unreasonable result. In affirming the Commission, the Circuit Court essentially utilized the same rationale.

Because the Legislature clearly intended in 1975 to eliminate the corporate deduction of federal income taxes, the Court of Appeals affirmed the Commission. The Court did not address NCR's constitutional challenge to the retroactive impact of the 1981 amendment because their statutory interpretation of the 1975 amendment renders the issue moot.

The taxpayer has not appealed this decision.

News/Sports Radio Network, Inc. and Wisconsin Independent Radio Network vs. Wisconsin Department of Revenue (Wisconsin Tax Appeals Commission, December 13, 1985). The issue for the Commission to determine was whether the taxpayers are entitled to consolidate their net incomes for purposes of 1980 and 1981 Wisconsin franchise tax returns.

During 1980 and 1981, News/Sports Radio Network, Inc. was a Wisconsin corporation which was engaged in the business of producing and selling short radio programs and radio feature stories to corporations or public relations agencies, which would provide them to radio stations for their use in exchange for "air time." Wisconsin Independent Radio Network was a Wisconsin corporation which produced programs for specific radio stations as well as commercials for advertising agencies.

The disputed assessments were made based upon (a) the department's "deconsolidation" of the income reported by both taxpayers on single Wisconsin franchise tax returns for the fiscal years ending October 31, 1980 and 1981 and (b) the department's "doomage" or estimated assessments against Wisconsin Independent Radio Network for the calendar years 1980 and 1981 for failure to file separate franchise tax returns from News/Sports Radio Network, Inc. The effect of the department's "deconsolidation" was to disallow to News/Sports Radio Network, Inc. losses attributable to Wisconsin Independent Network, Inc.'s operations for the two fiscal years in question.

In November 1979, News/Sports Radio Network, Inc. acquired the business assets of Wisconsin Independent Network, Inc. After this sale, Wisconsin Independent Network, Inc. retained corporate status and, therefore, its precise name was not available for use by News/Sports principals in incorporating a new entity.

In January of 1980, the principals of News/Sports Radio Network, Inc. incorporated Wisconsin Independent Radio Network, Inc. to preserve the name "Wisconsin Independent Network" as closely as possible. Articles of incorporation were filed with a certificate of incorporation which was received from the Wisconsin Secretary of State's office. Wisconsin Independent Radio Network never issued any capital stock, adopted any bylaws, appointed or elected officers or directors, or filed corporate annual reports with the Secretary of State, but separate books and a checking account were maintained for Wisconsin Independent Radio Network for purposes of assessing profitability of the operation and to protect News/Sports Radio Network, Inc.'s favorable financial rating for credit purposes.

News/Sports Radio Network, Inc. filed its 1980 and 1981 Wisconsin franchise returns together with a copy of its federal income tax returns for such periods. The income of News/Sports Radio Network, Inc. and Wisconsin Independent Radio Network were consolidated for federal and Wisconsin purposes. Each corporation maintained and listed on the returns separate employer numbers.

The taxpayers claimed that in order to protect the name "Wisconsin Independent Network" a paper subsidiary was formed. The corporate names "Wisconsin Independent Network, Inc." and "Wisconsin Independent News Network, Inc." were not available for use according to a determination by the Secretary of State, State of Wisconsin, and Wisconsin Independent Radio Network, Inc.'s name was approved on January 14, 1980; therefore, News/Sports Radio Network, Inc. as the parent corporation and Wisconsin Independent Radio Network as the subsidiary, filed Federal Forms 1122 and 851, consolidating both corporate returns into one return for the period under review.

The department contended that the taxpayers' filing of consolidated franchise tax returns for 1980 and 1981 fiscal years was not proper. Since each was a separate legal entity, which is beyond dispute, the doctrine of *Interstate Finance (Interstate Finance Corp. vs. Dept. of Taxation)*, 28 Wis. 2d 262 (1965)) requires separate returns. Thus, the department's removal of Wisconsin Independent Radio Network's net losses for 1980 and 1981 from News/Sports' franchise tax returns

was proper. The propriety of the department's imposition of franchise tax upon its estimate of Wisconsin Independent Radio Network's calendar year 1980 and 1981 income was not refuted.

The Commission held that Wisconsin Independent Radio Network, Inc., during the period under review, was a separate legal entity which was required to file a separate rather than a consolidated franchise tax return, irrespective of its economic interdependence with News/Sports Radio Network, Inc. The income reported as that of Wisconsin Independent Radio Network, Inc. cannot be used to compute News/Sports' franchise tax liability. Wisconsin Independent Radio Network failed to file its Wisconsin income tax returns for the years 1980 and 1981 and the department's doomage assessment is presumptively correct and the taxpayer failed to meet its burden of proof to show in what respects the department's action on its petition for redetermination was in error.

The taxpayers have not appealed this decision.

Star Line Trucking Corporation vs. Wisconsin Department of Revenue (Wisconsin Tax Appeals Commission, September 23, 1985). The sole issue for the Commission to decide was the proper year in which the taxpayer may write off the value of its motor carrier interstate operating rights.

The taxpayer is a motor carrier which, prior to July 1, 1980 and subsequently, had interstate operating authority licensed by the Interstate Commerce Commission (ICC).

On July 1, 1980, the Motor Carrier Act of 1980 (1980 Act) became effective deregulating motor carriers and making it easier for motor carriers to keep their licenses.

As a result of the Motor Carrier Act of 1980, the taxpayer sustained a deductible loss. The taxpayer claimed a loss of $79,178 for the tax year 1980. The department disallowed the claimed loss for 1980 but allowed an $87,549 deduction for this loss for the tax year 1981.

On December 19, 1980, the Financial Accounting Standards Board (FASB) issued "Statement of Financial Accounting Standards No. 44" addressing questions raised due to the enactment of the 1980 Act and requiring the unamortized cost of motor carrier intangible assets representing interstate operating rights to be charged to income and, if material, reported as an extraordinary item in the financial statements of motor carriers (the accounting theory upon which the deduction at issue is based).

The Securities and Exchange Commission (S.E.C.) by Release No. 150 issued December 20, 1973, adopted the principles, standards and practices promulgated by the FASB as having substantial support and thus acceptable accounting practices. Because of this 1973 Release, the S.E.C. is deemed to have accepted FASB No. 44 as of the day it was released, December 19, 1980.

During all relevant periods, the taxpayer was not regulated by the S.E.C.

By Accounting Series Circular No. 188, February 13, 1981, "Accounting for Intangible Assets of Motor Carriers to Accounting Officers of All Motor Carriers Subject to the Commissioner's Accounting and Reporting Regulations," the ICC adopted the requirements of FASB No. 44 ordering that "the accounting and reporting prescribed in this Circular shall be effective for the reporting year beginning January 1, 1980."

The Commission held that in Circular No. 188, the ICC specifically ordered that the policy adopted therein be "effective for the reporting year beginning January 1, 1980," and therefore, 1980 is the first year the write-off at issue was ordered pursuant to s. 71.04(8), Wis. Stats. The proper tax year in which the taxpayer is entitled to take the write-off at issue is the tax year 1980.

The department has not appealed this decision.

SALES/USE TAXES

Advance Pipe & Supply Co., Inc. and Milwaukee Sewer Pipe & Supply Co., Inc. vs. Wisconsin Department of Revenue (Court of Appeals, District IV, January 9, 1986). Advance Pipe & Supply Co. and Milwaukee Sewer Pipe & Supply Co. appealed from a judgment affirming a decision of the Wisconsin Tax Appeals Commission which assessed a sales tax on the companies' sales of manhole components. The issues were whether the taxpayers are real property construction contractors within the meaning of ss. 77.51(4)(i) and 77.51(18), Wis. Stats.; and if not, whether the Department of Revenue should be estopped from denying the taxpayers' status as real property construction contractors under the statutes. (See WTB #39 for a summary of the Circuit Court's decision.)

If the taxpayers are performing "real property construction activities" within the meaning of s. 77.51(18), Wis. Stats., then their purchases of raw materials are subject to the sales tax but their sales of precast manhole components to contractors are not taxable transfers. If, on the other hand, the taxpayers are manufacturers rather than real property contractors, their sales of manholes are subject to the sales tax, but their purchases of materials are not. The Commission concluded that the taxpayers did not meet the statutory definition and that their sales and deliveries of building materials to contractors are retail sales subject to taxation. As a result, the taxpayers are chargeable with collecting the appropriate tax and paying the proceeds to the department.

The Court of Appeals concluded that the taxpayers are operating as retailers who deliver building materials to plumbing and sewer contractors.

The taxpayers argued, however, that the department should be "equitably estopped" from denying their status as real property construction contractors. The argument is based on an April 1982 letter from the department stating that Advance Pipe was entitled to a refund for overpayment of sales tax. The taxpayers claim that they relied on the letter and thus, to their detriment, neither charged nor collected sales tax from their contractor-customers.

The department's letter to Advance Pipe neither acknowledges nor concludes that the taxpayers are involved in real property construction activities within the meaning of the tax laws. The refund was made solely on the basis of statements by Advance Pipe in its sales and use tax return that it was engaged in such activities. The return did not describe Advance Pipe's activities; it stated simply that its sales were "generated primarily from real construction activity and are not subject to sales tax." The department accepted Advance Pipe's representation as true,

and its failure to challenge the return or perform an audit at that time should not preclude it from later revising its position after investigating the company's actual operations.

The Court of Appeals agreed with the Circuit Court that: "The taxpayers . . . were not relying upon statements made by the Department. Indeed, the Department was relying upon statements made by Advance Pipe." The taxpayers have not shown the existence of the elements of estoppel; nor have they established that the department's actions were unconscionable.

The taxpayers have not appealed this decision.

Frisch, Dudek and Slattery, Ltd. vs. Wisconsin Department of Revenue (Circuit Court of Dane County, December 26, 1985). The issue in this case was whether the taxpayer's charges to clients for photocopies are subject to the sales tax contained in s. 77.52(1), Wis. Stats. The Wisconsin Tax Appeals Commission affirmed the department's decision imposing sales tax on photocopying charges billed by Frisch, Dudek and Slattery to their clients during the period from January 1, 1975 to October 31, 1979. (See WTB #39 for a summary of the Wisconsin Tax Appeals Commission's decision.)

The taxpayer is an incorporated law firm engaged solely in the practice of law. When billing its clients for legal services, the taxpayer itemizes certain out-of-pocket expenses and bills these separately from its flat hourly rate. During the time period in question, the taxpayer charged clients either $.20 or $.25 per photocopy, except for large orders which were farmed out to independent operators who charged substantially less per copy. The average cost to the taxpayer over the period in question was $.23 per copy.

The applicability of the sales tax was recently examined by the Court in *Kollasch v. Adamany,* 104 Wis. 2d 552 (1981). There the Court noted a circularity between s. 77.52 and s. 77.51, Wis. Stats., which contains definitions for the terms used in s. 77.52. The Court attempted to formulate a workable definition of the term "retailer" because it felt the statutory definition was ambiguous. The Court noted, "the common conception of a retailer, as shown by the dictionary definition, is one who transacts business with a consumer in hopes of making a profit on the transaction." The Court also noted that the taxability of a particular sale depends upon the specific circumstances of the transaction.

Applying this definition of a retailer to the facts of the transactions which occurred here, it is clear that the sales are not taxable. The transfer of photocopies by the taxpayer to its clients and others is not done with a profit motive in mind. The real purpose of the transactions is to complement the efficient rendering of legal services. Without the provision of legal services there would be no photocopies.

Further support for the conclusion that the transfer of photocopies is not a taxable transaction is found in section Tax 11.67 Wis. Adm. Code (1981) which provided:

> (1) GENERAL. When a transaction involves the transfer of tangible personal property along with the performance of a service, *the true objective of the purchaser must be considered to determine whether such transaction is a sale of tangible personal property or the performance of a service with the transfer of property being merely incidental to the performance of the service.* If the objective of the purchaser is to obtain the personal property, a taxable sale of that property is involved. However, if the objective of the purchaser is to obtain the service, a sale of a service is involved even though, as an incidence to the service, some tangible personal property may be transferred. Thus, a person performing business advisory, recordkeeping, payroll and tax services for small businesses is providing a service. Such person is the consumer, not the seller, of property such as forms and binders which furnishes without separate charge as an incidence to the service.

The obvious objective of the purchasers here was to obtain legal services.

The department argued that this provision must be ignored because it is impossible to determine the motives of the taxpayer's clients when they purchase photocopies. However, the record makes clear that copies were only provided to the taxpayer's legal clients and then at a cost of four to five times the price which clients could have purchased the copies from other sources. This is sufficient evidence to draw the conclusion that no one dealt with the taxpayer solely for the purpose of procuring photocopies.

The Circuit Court concluded that the department has erroneously interpreted s. 77.52, Wis. Stats., and that a correct construction compels the conclusion that the taxpayer is not a retailer selling personal property.

The Commission's decision and order should be modified as follows. During the period under review, the taxpayer was not a "retailer" of photocopies as the word is defined by statute and case law. The taxpayer was a provider of legal services, a service not subject to the Wisconsin sales tax. The taxpayer's furnishing clients with photocopies were transfers of tangible personal property incidental to and in conjunction with sales of a nontaxable service. The true objective of the taxpayer was to sell the taxpayer's legal services. Its billings were for a nontaxable service, which was the true objective of its clients, and not for the sale of tangible personal property although some tangible personal property was transferred as an incidence to providing the service.

The department has appealed this decision to the Court of Appeals.

Montgomery Ward & Co., Inc. vs. Wisconsin Department of Revenue (Wisconsin Tax Appeals Commission, November 29, 1985). Montgomery Ward & Co., Inc. (Ward) is an Illinois Corporation with its principal place of business and corporate domicile located in Chicago, Illinois. Its principal business activity is that of retail merchant. Ward conducts this business activity in the State of Wisconsin through retail outlets, catalog stores, catalog agencies and direct mail catalog sales. This was the case throughout the period in issue, September 1, 1969 through January 31, 1981.

Direct mail catalog sales were made by Ward customers by mailing completed catalog order forms to Ward catalog house locations where goods were withdrawn from inventory and sent back to the customers by mail. Residents of Wisconsin ordered goods by mail from Ward's catalog houses in Chicago, Illinois and St. Paul, Minnesota. Prices in the

catalog were quoted F.O.B. the catalog house and did not include charges for shipping and handling. On cash orders the customer computed and prepaid transportation charges for mailing the goods from the catalog house to his or her residence in Wisconsin. Ward would compute this amount for its charge account customers and added it to the invoice as a separate charge. The completed order form, together with payment for cash orders, was placed in the U.S. mails in Wisconsin by the customer. The order was accepted and the sales price collected at the out-of-state catalog house location where the goods were taken from inventory and packaged for shipment. Shipment was made from a point outside Wisconsin where the goods were deposited in the U.S. mails for delivery to the Wisconsin buyer.

During the period at issue, Ward did not collect Wisconsin sales or use tax on the transportation charges it charged and remitted Wisconsin tax only on the price of the item of merchandise being sold, which it reported as "use" tax rather than "sales" tax.

In the case of all such sales, the Wisconsin customers first obtained personal possession of the item purchased when the United States Postal Service or the common carrier delivered the item to the customer's home.

On April 8, 1976, the department issued to Ward a notice of additional sales and use tax and penalty for the period September 1, 1969 through October 31, 1975. Included was an assessment on an "Additional Measure of Sales Tax-Transportation Charges on Mail Order Sales" from the St. Paul and Chicago mail order houses. In addition, a 25% negligence penalty was imposed under s. 77.60(3) based only on additional sales tax and not on the entire assessment including use tax. Ward filed a timely petition for redetermination of the assessments on May 13, 1976, which was granted in part by reversing the negligence penalty and otherwise denied by the department on October 1, 1976.

On March 5, 1980, the department issued to Ward a notice of sales and use tax deficiency determination for the period November 1, 1975 through January 31, 1976. Again, an adjustment was made for transportation charges billed by Ward in its direct mail sale of merchandise, determined by the department to be subject to sales tax under Wis. Adm. Code section Tax 11.94.

On June 17, 1982, the department issued to Ward a notice of sales and use tax deficiency determination covering the period February 1, 1976 through January 31, 1981. Among the various adjustments made was another for inclusion of sales tax on transportation charges billed by seller in its direct mail sales of merchandise from Chicago and St. Paul mail order houses. Also, a 25% negligence penalty under s. 77.60(3) was imposed.

The only disputed adjustments remaining were as follows:

A. The department's sales taxation of transportation charges billed in conjunction with mail order merchandise sales shipped from outside Wisconsin to Wisconsin customers for the period September 1, 1969 through January 31, 1981.

B. The department's use of a 12% interest rate on the June 17, 1982 assessment covering the period February 1, 1976 through January 31, 1981.

C. The department's imposition of a 25% negligence penalty under s. 77.60(3) applied to selected amounts relating to specific adjustments rather than the entire amount assessed for the period February 1, 1976 through January 31, 1981.

Excluded from the measure of the tax upon which the penalty under review was imposed were certain additional sales made by Ward which were determined to be taxable in the field audit, but for which Ward had accepted invalid exemption certificates; transportation charges on direct mail order sales which are at issue in this proceeding; newspaper inserts; and catalogs distributed from an out-of-state printer directly to the home of Wisconsin customers by mail. Both of the latter matters were the subject of litigation at the time regarding whether a retailer's use of such inserts and catalogs was subject to the use tax.

The department has a policy that authorizes imposition of the negligence penalty on only a portion of the additional tax assessed. The policy was adopted in the interest of equity since, in some cases, some transactions are not properly reported for reasons other than neglect such as reasonable differences of opinion in the interpretation of the tax law held by the taxpayer on one hand and the Department of Revenue on the other, while at the same time, other items were not reported due to neglect.

The 25% negligence penalty was imposed upon the following items of sales and use tax adjusted: Catalogs, Fixed Assets, Supplies, Contract Installation, Border Stores, Catalog Desks and Bad Debts.

Among the major items assessed, the "Catalogs" adjustment related to failure to properly estimate use tax for catalogs sold over the counter for fiscal 1979 and 1980 and failure to self-assess any use tax for fiscal 1977, 1978 and 1981. The unreported sales involved approximately $2.6 million for the five-year period. Ward's explanation was that its procedure was to pay the use tax once a year because it could not determine the amount to be estimated until after the close of the fiscal year. On the other hand, the taxpayer contended that use tax accruals were made on a monthly basis on the corporate books. No satisfactory explanation was furnished for failure to make proper estimates in three years or any estimates in two years.

The "Border Stores" adjustment related to sales made by Ward's retail stores in Duluth and St. Paul, Minnesota, which were delivered by truck to customers in Wisconsin. Such sales were exempt from Minnesota sales taxation and Ward had procedures directing sales/use tax to be paid to the state of delivery. No satisfactory explanation was offered for failure to report these sales for the fiscal years 1977 through 1981 in the total amount of approximately $1.6 million.

The "Catalog Desks" adjustment relates to unreported taxable sales from store catalog desks of six retail stores for the month June 1980 in the total amount of $165,212. No satisfactory explanation was offered for failure to report these sales.

The "Bad Debts" adjustment resulted from Ward improperly including finance charge amounts in reducing gross receipts for bad debts, thus overstating the reduction in taxable gross receipts. Finance charges were not segregated on the bad debt documents used to prepare the re-

turns. No satisfactory explanation for this error was made.

The Commission held as follows:

A. Throughout the period in question, Ward was a "retailer" within the meaning of s. 77.51(7), Wis. Stats., and a "retailer engaged in business in this state" within the meaning of s. 77.51(7g), Wis. Stats., and subject to Wisconsin's sales and use tax jurisdiction.

B. The separately stated cost of transportation included as charges in Ward's mail order sales to Wisconsin customers from its Chicago, Illinois and St. Paul, Minnesota catalog houses was "cost of transportation of the property prior to its sale to the purchaser" and includable, therefore, as "gross receipts" within the meaning of ss. 77.51(11)(a)3 and (4r), Wis. Stats., subject to the Wisconsin retail sales tax of 4% under s. 77.52(1), Wis. Stats.

C. Such transportation charges also constituted "the cost of transportation of the property prior to its purchase" and were includable in the "sales price," within the meaning of ss. 77.51(12)(a)3 and (4r), Wis. Stats., subject to the 4% Wisconsin use tax under s. 77.53(1), Wis. Stats. If such sales were taxable under the sales tax provisions, they are exempt from use tax under s. 77.56(1), Wis. Stats. If such sales were not taxable under sales tax provisions, they were taxable under the use tax statutes, which Ward was required to collect under ss. 77.51(7g) and 77.53(3), Wis. Stats.

D. The 12% interest rate on unpaid sales and use taxes under s. 77.60(1), Wis. Stats., as amended by Laws of 1981, Chapter 20, Section 1125hm applies to all assessments made on or after August 1, 1981, "regardless of the taxable period to which they pertain." This Commission has construed parallel language pertaining to interest on income and franchise taxes to require the 12% rate to cover all the years those taxes have been outstanding, or in other words, from the original due date. The June 17, 1982 assessment of sales and use tax is thus subject in its entirety to 12% interest rate.

E. The Commission is not a constitutionally mandated judicial body and is, therefore, without the power to rule on the constitutional validity of any duly enacted statute.

F. The burden was on Ward to prove that the errors in the incorrect sales/use tax returns filed were due to good cause and not due to neglect. Ward failed to meet that burden with respect to those errors which the department deemed due to neglect. Such penalties were, therefore, properly imposed. Nothing in the controlling statute requires that the penalty be applied to the entire assessment.

The taxpayer has appealed this decision to the Circuit Court.

James M. Salmon d/b/a General Lighting and Maintenance vs. Wisconsin Department of Revenue (Wisconsin Tax Appeals Commission, November 29, 1985). The assessment in dispute before the Commission imposed a sales and use tax on the cleaning and maintaining of fluorescent lighting fixtures, lamps or chandeliers in offices.

The department maintained that the taxpayer's cleaning, servicing and maintenance of lighting facilities is subject to sales and use tax under the provisions of s. 77.52(2)(a)10, Wis. Stats. The taxpayer contended that the personal property it consumed and the repair and maintenance services it performed became a part of the real estate and were not subject to tax.

During the period involved, 1977 through 1980, the taxpayer held a seller's permit and specialized in the cleaning, maintenance and replacement of lamps in free-hanging and built-in lighting facilities. The taxpayer collected sales taxes on the lamps he installed but not on the labor expended to install them or on the other maintenance services he performed.

The Commission concluded that the taxpayer's cleaning, maintenance and replacement of lamps and lighting systems for commercial customers in the Milwaukee area during the period under review constituted servicing tangible personal property in the form of "office, restaurant and tavern type equipment including by way of illustration but not of limitation lamps, chandeliers. . ." as those terms are used in s. 77.52(2)(a)10, Wis. Stats., and the gross receipts received from those services are subject to tax. The services the taxpayer performed retained their character as tangible personal property subject to tax per the clear and unambiguous language contained in s. 77.52(2)(a)10, Wis. Stats.

The taxpayer has not appealed this decision.

Senior Golf Association of Wisconsin, Inc. vs. Wisconsin Department of Revenue (Court of Appeals, District IV, November 5, 1985). The Senior Golf Association of Wisconsin, Inc. appealed an order affirming a Wisconsin Tax Appeals Commission ruling concerning its sales tax liability. The association, a nonprofit corporation, exists to organize golf outings for its members. The outings occur at various private clubs, and members pay a negotiated fee to the clubs to participate in each event. Nonmembers are excluded. The issue is whether s. 77.52(2)(a)2, Wis. Stats., allows the state to impose a sales tax on the association's initiation and dues payments, which it uses to pay administrative costs. (See WTB #38 for a summary of the Circuit Court's decision.)

Section 77.52(2)(a)2 imposes a tax on receipts from the sale of access to athletic or recreational facilities. The association argued that the members purchase access to the facilities through the charges for the individual outings, not through the dues and initiation fees. It also contended that it cannot sell access to facilities it does not own. The department responded that the initiation and dues payments are also access charges and therefore taxable because nonmembers are excluded from the outings.

The Court of Appeals concluded that the association's initiation fees and dues payments are clearly taxable under the statute. The essential question under s. 77.52(2)(a)2 is whether the association's members must pay these charges to gain access to the golf courses. The answer is that they must because nonmembers may not participate in the outings. The statute makes no distinction where the organization does not own the recreational facility, or only uses the charges to pay administrative costs.

The taxpayer has not appealed this decision.

Troyanek's Tap & Line Service, Inc. vs. Wisconsin Department of Revenue (Wisconsin Tax Appeals Commission, November 1, 1985). During

the period involved, the taxpayer was in the business of cleaning beer taps and lines in taverns and bars located in the LaCrosse, Wisconsin area.

During the calendar years 1979, 1980, 1981, 1982, 1983 and January-August 1984, the taxpayer received payment for its services which it reported on its Wisconsin corporate franchise or income tax returns. The taxpayer, however, did not file Wisconsin sales tax returns or pay Wisconsin sales or use taxes on the gross receipts it received during that period of time.

Under date of September 28, 1984, the department issued notices of sales and use taxes due against the taxpayer covering the calendar years 1979, 1980, 1981, 1982, 1983 and January-August 1984 totaling $14,881.70. The assessments imposed a sales and use tax on the gross receipts the taxpayer received from its beer tap and line cleaning operation during the period involved.

The assessments resulted from an audit the department conducted on the G. Heileman Brewing Company of LaCrosse, Wisconsin during which it discovered that the taxpayer was not reporting or paying sales taxes on the gross receipts it received from its beer tap and line cleaning operations.

The taxpayer was not aware it had a sales and use tax liability until the assessments were made in September of 1984. It did not collect sales and use tax from its customers during the period under review.

The taxpayer objected to the assessments on the following basis:

A. Its services are not subject to tax.

B. It relied on the advice of its attorney and accountant.

C. The department should have notified them of its sales and use tax obligation at an earlier date.

D. It can't afford to pay the assessments.

The Commission held as follows:

A. The taxpayer's cleaning of beer tap and line equipment in taverns and bars in the LaCrosse, Wisconsin area during the period under review constituted servicing tangible personal property in the form of "bar equipment" and/or "restaurant and tavern type equipment" as those terms are used in s. 77.52(2)(a)10, Wis. Stats., and the gross receipts received from those services during the period under review were subject to tax.

B. The taxpayer's reliance on advice it received from its attorney and accountant does not relieve it from the sales and use tax liability arising from the provisions of Wisconsin's sales and use tax law.

C. Wisconsin sales and use tax law is based on a self-reporting and self-assessment system with the primary responsibility for compliance resting with the taxpayer, not the Wisconsin Department of Revenue.

D. Ability to pay is not a valid criteria to determine liability under Wisconsin sales and use tax law.

The taxpayer has not appealed this decision.

Wisconsin State Telephone Association, et al. vs. Mark E. Musolf and Wisconsin Department of Revenue (Circuit Court of Dane County, October 31, 1985). This matter was before the Circuit Court on the defendants' motion for summary judgment. The plaintiffs are domestic and foreign corporations and cooperatives, as well as the telecommunications trade association, and they provide or purchase telephone services within Wisconsin. They claimed that s. 77.52(2)(a)4, Wis. Stats., which forces them to pay a 5% sales tax on the gross receipts from all interstate and international telephone calls originating from and charged to telephones located in Wisconsin, violates their substantive due process rights guaranteed by the constitution.

In *Wisconsin Tel. Co. v. Dept. of Revenue,* 125 Wis. 2d 339 (Ct. App. 1985), the Court of Appeals rejected a challenge to s. 77.52(2)(a)4, Wis. Stats., brought on commerce clause grounds. The question before the Circuit Court now is whether this rejection is fatal to the plaintiffs' due process challenge. The plaintiffs have contended that the *Wisconsin Tel. Co.* case does not control this case because a due process challenge requires a different approach to the issues than a commerce clause challenge. The plaintiffs' final argument is that the *Wisconsin Tel. Co.* court did not consider the effect of the tax on out-of-state telephone companies.

The Circuit Court concluded that the *Wisconsin Tel. Co.* case controls the instant case and summary judgment in favor of the defendants must be granted.

The plaintiffs have not appealed this decision.

Wisconsin Telephone Company, et al. vs. Wisconsin Department of Revenue, et al. (Wisconsin Supreme Court, November 5, 1985). The taxpayers appealed the adverse decision of the Court of Appeals, District IV, which held the sales tax imposed by s. 77.52(2)(a)4, Wis. Stats., constitutional. (See WTB #44 for a summary of the decision of the Court of Appeals.)

The Supreme Court denied the taxpayers' petition for review.

TAX RELEASES

("Tax Releases" are designed to provide answers to the specific tax questions covered, based on the facts indicated. However, the answer may not apply to all questions of a similar nature. In situations where the facts vary from those given herein, it is recommended that advice be sought from the Department. 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.)

Individual Income Taxes

1. Adoption Expense Deduction

Corporation Franchise/Income Taxes

1. Sales Factor: Items of Income Includable
2. Deductibility of Motor Carriers' Operating Authorities
3. Bad Debts - Savings and Loan Associations
4. Nexus and Certain Exempt Activities for Foreign Corporations

5. Wisconsin Tax Treatment of Deferred Income by Corporations
6. Doctrine of Recoupment in Pending Cases Where Taxpayer Has Paid an Admitted Portion of Tax

Sales/Use Taxes

1. Furnaces That May Be Used to Burn Bio-Mass Pellets or Lignite Fuel

INDIVIDUAL INCOME TAXES

1. Adoption Expense Deduction

Statutes: sections 71.02(2)(f) and 71.05(1)(b)7, 1983 Wis. Stats.

Note: This Tax Release applies only with respect to taxable years 1978 through 1985.

Facts: Section 71.05(1)(b)7, 1983 Wis. Stats., provides for a subtraction from federal adjusted gross income for amounts expended by an adoptive parent or prospective adoptive parent in adoption fees, court costs or legal fees relating to the adoption of a child, whether or not the adoption process is completed. The deduction is allowed to the extent that the adoption costs, when added to allowable medical deductions under Section 213 of the Internal Revenue Code (IRC), exceeds 5% of the person's federal adjusted gross income.

Section 71.02(2)(f), 1983 Wis. Stats., defines "itemized deductions" as deductions from federal adjusted gross income allowable under the IRC in determining federal taxable income with certain exceptions. This statute also provides that part-year residents must prorate itemized deductions on the basis of Wisconsin adjusted gross income to federal adjusted gross income.

A taxpayer is a Michigan resident until November 1, 1985 at which time the taxpayer moves to Wisconsin. In February of 1985, prior to the move to Wisconsin, the taxpayer incurs and pays adoption expenses. The expenses include a required payment to an adoption agency for reimbursement of the mother's hospital and medical expenses.

Question 1: Does the amount paid for reimbursement of the mother's hospital and medical expenses qualify as an adoption expense for Wisconsin tax purposes?

Answer 1: Yes. Pursuant to s. 71.05(1)(b)7, 1983 Wis. Stats., any amount expended by an adoptive parent in adoption fees, court costs or legal fees relating to the adoption of a child is deductible for Wisconsin income tax purposes (subject to income limitations). A legal obligation to pay for the hospital and medical expenses of the mother may be considered adoption fees.

Question 2: Is a part-year resident allowed a deduction for adoption expenses paid prior to the move to Wisconsin?

Answer 2: Yes. Section 71.05(1)(b)7, 1983 Wis. Stats., does not limit the subtraction for adoption expenses to full year residents.

Question 3: Is a part-year resident required to prorate the subtraction for adoption expenses?

Answer 3: No. Section 71.02(2)(f) provides that part-year residents must prorate itemized deductions. Even though the allowable deduction for adoption expenses is computed based on the adoption costs added to medical expenses allowable as an itemized deduction, the adoption expenses claimed as a subtraction from Wisconsin income are not deductions allowable under the IRC. Therefore, the adoption expenses do not meet the definition of an "itemized deduction" and do not need to be prorated when claimed by a part-year resident.

(Note: Federal law does allow an itemized deduction up to $1,500 for qualified adoption expenses relating to the adoption of a child with special needs. If an adoptive parent who is a part-year resident claims this itemized deduction for the adoption of a child with special needs for Wisconsin purposes the deduction would have to be prorated along with any other itemized deductions claimed.)

CORPORATION FRANCHISE/INCOME TAXES

1. Sales Factor: Items of Income Includable

Statutes: sections 71.07(1m), (2)(c), (cm) and (cr), 1983 Wis. Stats. as amended by 1985 Wisconsin Act 120

Wis. Adm. Code: section Tax 2.39(5), September 1983 Register

I. INTRODUCTION:

The May 9, 1985 Wisconsin Tax Appeals Commission decisions in *United States Steel Corporation vs. Wisconsin Department of Revenue* and *International Business Machines Corporation vs. Wisconsin Department of Revenue* altered the Wisconsin sales factor computation under s. 71.07(2)(c), Wis. Stats., and Wis. Adm. Code section Tax 2.39(5). 1985 Wisconsin Act 120 reversed in part the effect these decisions had on the sales factor computation. This Tax Release will review the May 9, 1985 decisions by the Wisconsin Tax Appeals Commission as they are related to the sales factor issue, what items of income are includable in the sales factor based on the *U.S. Steel* and *IBM* decisions, and the effects of 1985 Wisconsin Act 120 on the sales factor computation, including choosing the option to apply this Act to tax years prior to the 1986 taxable year.

This Tax Release is intended only to set forth what items of apportionable business income are included in the sales factor. It is not intended to answer whether an item of income is apportionable or nonapportionable or unitary or nonunitary. The treatment under Parts II.B and C and III.B is applicable only if the items of income are unitary and apportionable.

CAUTION - This Tax Release has no application to insurance companies, interstate air carriers, interstate motor carriers, interstate pipeline companies or interstate finance companies. These corporations apportion their incomes using different statute sections or tax rules.

II. SALES FACTOR - INTERPRETATION AS A RESULT OF *U.S. STEEL* AND *IBM* DECISIONS:

A. DECISIONS BY THE WISCONSIN TAX APPEALS COMMISSION - MAY 9, 1985

(1) *United States Steel Corporation vs. Wisconsin Department of Revenue*

(2) *International Business Machines Corporation vs. Wisconsin Department of Revenue*

Although these cases involve several issues, only the portion dealing with the items of income includable in

the computation of the sales factor is being covered by this Tax Release.

In these companion decisions the Commission held that apportionable incomes from intangibles—dividends, interest, royalties from patents and the gross proceeds from the sale, exchange and redemption of the taxpayers' intangible investments—must be included in the denominators of their Wisconsin sales factors. (1975 was the last tax year in both of these cases.)

The Commission also found that certain dividends received were from nonunitary affiliates, and were, accordingly, not includable in apportionable income; therefore, these dividends were not includable in the sales factor denominator.

The question of what portion (gross or net) of dividends deductible under s. 71.04(4)(a) or (b), Wis. Stats., is includable in the sales factor was not an issue in the *U.S. Steel* and *IBM* cases. However, in its February 17, 1986 Order of Rehearing in the case of *American Telephone and Telegraph Company vs. Wisconsin Department of Revenue*, the Wisconsin Tax Appeals Commission held that the amount of dividend income deducted under s. 71.04(4)(a) or (b), Wis. Stats., was not includable in the sales factor. Instead, only the net amount not deductible is includable in the factor.

The Department did not appeal these decisions and is bound by them, including the sales factor computations under s. 71.07(2)(c), Wis. Stats. These decisions have retroactive application to all years open to assessment under s. 71.11(21), 1983 Wis. Stats., or refund under s. 71.10(10), 1983 Wis. Stats., or their counterparts for the years involved, prior to taxable year 1986. For taxable years 1986 and thereafter the sales factor must be computed under ss. 71.07(2)(c), (cm) and (cr), Wis. Stats., as described in Part III below.

B. EXAMPLES OF INTANGIBLE INCOMES WHICH ARE INCLUDABLE (IF UNITARY AND APPORTIONABLE) OR NOT INCLUDABLE IN THE SALES FACTOR AS A RESULT OF THE *U.S. STEEL* AND *IBM* DECISIONS

	Includable	Not Includable
(1) Denominator of Sales Factor		
(a) All income from nonunitary affiliates which is not taxable		X
(b) Exempt income—e.g., life insurance proceeds in payment of a death claim		X
(c) Dividends from DISCs excludable under s. 71.11(7r)		X
(d) Dividends deductible under s. 71.04(4)(a) or (b)		X
(e) All other apportionable dividends not included in items (c) or (d) above	X	
(f) Apportionable interest income	X	
(g) Royalties from patents	X	
(h) Gross receipts from dispositions of investments in nonunitary affiliates		X
(i) Gross receipts from dispositions (sales, exchanges or redemptions) of all other intangible assets (other than item (h) above) includable in apportionable income	X	
(j) Corporation's distributive share of the net income (not losses) from limited partnerships	X	

(2) Numerator of Sales Factor

As noted above, these decisions dealt with a number of issues, including the question of what items of income were includable in the denominators of the sales factors. They did not address the question of what items of income are included in the numerator of the sales factor since the Department had taken the position that such items of intangible income were not includable in the sales factor at all.

It is the Department's position that intangible incomes cited under Part II.B.(1), above, which are included in the denominator are also includable in the numerator of the sales factor if the income-producing activity is in Wisconsin. ("Income-producing activity" is based on direct cost of performance in jurisdiction states if such income-producing activity is performed both in and outside Wisconsin pursuant to s. 71.07(2)(c)3, Wis. Stats.) This position applies to any year open to assessment or refund prior to the 1986 taxable year.

C. OTHER TYPES OF APPORTIONABLE INCOME INCLUDABLE IN THE SALES FACTOR AS A RESULT OF THE *U.S. STEEL* AND *IBM* DECISIONS

Total Company Denominator	Includable In The Wisconsin Numerator?
(1) Gross receipts from dispositions of real estate	Yes, if the real estate is located in Wisconsin
(2) Gross rents and royalties from real estate and tangible personal property	Yes, if the real estate or tangible personal property is located in Wisconsin
(3) Gross receipts of farms, mines and quarries	Yes, based on rule Tax 2.39(5)
(4) Gross receipts from management fees to third parties or at arm's-length price to affiliates (see Part II.D.(2) below), franchise fees and personal services	Yes, if income-producing activity is performed in Wisconsin (based on direct cost of performance if both in and outside Wisconsin)
(5) Gross receipts from sales of tangible personal property. Examples include: (a) Sales of finished goods inventory (b) By-product sales (c) Scrap sales (d) Sales of assets used in the production of business income (e) Gains or losses on foreign currency transactions involving the *export* of goods (an adjustment to selling price which may occur when such selling price is stated in foreign currency)	Yes, based on rule Tax 2.39(5) except that gains or losses on foreign currency transactions involving the export of goods are not includable
(6) All other apportionable gross receipts. Examples include: (a) Sales of accounts receivable to factors (does not include normal collections of accounts receivable) (b) Fees earned by an agent in connection with the issuance of commercial paper (c) Amounts received from damages, judgments or antitrust awards	Yes, for items (a) and (b), if income-producing activity is performed in Wisconsin (based on direct cost of performance if both in and outside Wisconsin). For item (c) and other apportionable gross receipts, the answer depends on the factual situation; write to the address listed below at Part IV
(7) Receipts from installment sales (if permissible under rule Tax 2.19) in the year of collection (if not permissible as an installment sale, receipts are reportable in the year of sale)	Yes— *Tangible property* - based on rule Tax 2.39(5) *Intangible property* - if the income-producing activity is performed in Wisconsin
(8) Gross receipts of the above items by general partnerships (corporation's distributive share only)	Yes, includable as noted above for applicable item(s)

D. EXAMPLES OF ITEMS NOT INCLUDABLE IN THE SALES FACTOR AS A RESULT OF THE *U.S. STEEL* AND *IBM* DECISIONS

(1) Receipts from the sale of securities (e.g., stocks or bonds) of the issuing corporation by the issuing corporation.

(2) Reimbursement of administrative expenses allocated to an affiliate regardless as to how classified on the books. (See Part II.C.(4) above.)

(3) Gains or losses on foreign currency transactions involving the *import* of goods (an adjustment of cost, not a gross receipt).

(4) Cash discounts earned on purchases (an adjustment of cost, not a gross receipt).

(5) Uncashed checks restored to books.

(6) Recoveries of items previously deducted, including bad debts, taxes, freight and insurance.

III. SALES FACTOR - COMPUTATION UNDER 1985 WISCONSIN ACT 120:

A. BACKGROUND

1985 Wisconsin Act 120 significantly changes the computation of the sales factor for multistate apportionment corporations. The Act amends s. 71.07(2)(d)1, repeals and recreates s. 71.07(1m), and creates s. 71.07 (2)(cm) and (cr). It specifies what income is apportionable and what is nonapportionable, as well as which items of income are included and which are not included in the sales factor calculation.

This legislation reverses the effect of the *U.S. Steel* and *IBM* Wisconsin Tax Appeals Commission decisions by excluding apportionable income from intangibles from the sales factor, except for certain royalties and franchise fees from income-producing activities. This legislation first applies to the taxable year 1986, but, at the taxpayer's option, may be applied retroactively to all years which are open to assessment or refund. Taxpayers exercising this option must apply it to all years prior to the 1986 tax year that are open to assessment or refund. Notification to the Department must be in writing. (See Part III.D below.)

B. ITEMS OF INCOME INCLUDABLE IN SALES FACTOR - S. 71.07(2)(cm)

Pursuant to s. 71.07(2)(cm) as created by 1985 Wisconsin Act 120, "sales" as used in s. 71.07(2)(c), Wis. Stats., includes, but is not limited to, the following items related to the production of business income:

(1) Gross receipts from the sale of inventory.

(2) Gross receipts from the operation of farms, mines and quarries (for the taxable year 1982 and thereafter).

(3) Gross receipts from the sale of scrap or by-products.

(4) Gross commissions.

(5) Gross receipts from personal and other services.

(6) Gross rents from real property or tangible personal property.

(7) Interest on trade accounts and trade notes receivable.

(8) A general partner's share of the partnership's gross receipts.

(9) Gross management fees.

(10) Gross royalties from income-producing activities.

(11) Gross franchise fees from income-producing activities.

C. ITEMS OF INCOME NOT INCLUDABLE IN SALES FACTOR - S. 71.07(2)(cr)

Pursuant to s. 71.07(2)(cr), as created by 1985 Wisconsin Act 120, the following items are among those that are not included in "sales" as used in s. 71.07(2)(c), Wis. Stats.:

(1) Gross receipts and gain or loss from the sale of tangible business assets, except those under s. 71.07(2) (cm) 1, 2 and 3.

(2) Gross receipts and gain or loss from the sale of nonbusiness real or tangible personal property.

(3) Gross rents and rental income or loss from real property or tangible personal property if that real property or tangible personal property is not used in the production of business income.

(4) Royalties from nonbusiness real property or nonbusiness tangible personal property.

(5) Proceeds and gain or loss from the redemption of securities.

(6) Interest, except interest under s. 71.07(2) (cm) 7, and dividends.

(7) Gain or loss from the sale of intangible assets.

(8) Dividends deductible under s. 71.04(4).

(9) Gross receipts and gain or loss from the sale of securities.

(10) Proceeds and gain or loss from the sale of receivables.

(11) Refunds, rebates and recoveries of amounts previously expended or deducted.

(12) Other items not includable in apportionable income.

(13) Foreign exchange gain or loss.

(14) Royalties and income from passive investments.

(15) A limited partner's share of income or loss from a partnership.

D. OPTION TO APPLY SALES FACTOR COMPUTATION UNDER 1985 WISCONSIN ACT 120 TO TAX YEARS PRIOR TO 1986

(1) Years For Which Option May Be Applied

Although the sales factor computation under 1985 Wisconsin Act 120 first applies to the 1986 taxable year, taxpayers may, at their option, elect to apply this legislation retroactively to all years prior to 1986 which are open to assessment or refund. This means years open for assessment under s. 71.11(21), or open for refund under s. 71.10(10), including contested assessments, refunds and refund claim denials which have not yet been acted on by the Department of Revenue's Appellate Bureau. If a net business loss offset from a closed year is carried forward into an open year, the loss year is not an open year for purposes of this option.

The option to apply s. 71.07(2)(cm) and (cr), Wis. Stats., to years prior to 1986 may be exercised by the taxpayer at any time so long as the "open" years affected have not been finalized by any of the various statutes of limitation. Once an option is exercised, it must be consistently applied to all years which are open to assessment or refund at that time. Such option may be subsequently changed only if all years for which it was initially exercised are also changed. The following examples illustrate years for which the option may be applied:

(a) Taxpayer A, a calendar year corporation, filed its Wisconsin franchise/income tax returns each year before March 15 of the succeeding year, reporting net income each year. The taxpayer files a sales factor option on May 1, 1986. After March 17, 1986, the year 1981 is not open to assessment or refund so the only years affected by the option are the years 1982 through 1985.

(b) Taxpayer B, a calendar year corporation with a similar filing record, was field audited for the years 1977 through 1979, which resulted in an assessment. A petition for redetermination was filed with the Appellate Bureau, and no action has been taken to date.

Taxpayer B files a sales factor option on September 15, 1986. The contested assessment on the years 1977 through 1979 at the Appellate Bureau keeps those years open. The years 1982 through 1985 are open under ss. 71.10(10) and 71.11(21). The taxpayer may not exercise the option for 1980 and 1981 after March 17, 1986 as those years are no longer open for adjustment or refund under the statute. Thus the computation of the sales factor under the option will be made for the years 1977 through 1979 and 1982 through 1985.

(c) Taxpayer C, another calendar year corporation with a similar filing record, reported the following amounts, before business loss carry forwards:

1981	$(2,000)
1982	(1,500)
1983	500
1984	3,500
1985	3,000

Taxpayer C files a sales factor option on January 15, 1987. Because the 1981 business loss may be carried forward to 1983 and 1984 the loss may be adjusted, but the year is not open for assessment or refund. Therefore, the taxpayer may not exercise the option to recompute the 1981 sales factor. Exercising the option will require that the sales factor for the years 1982 through 1985 all be recomputed under s. 71.07(2)(cm) and (cr), 1985 Wis. Stats.

(d) Taxpayer D, a calendar year corporation, was field audited for the years ended December 31, 1981 through December 31, 1983. Additional tax was assessed in each year, and the assessment was paid in October of 1985. Only taxable years 1984 and 1985 are open and could be affected by the option.

(e) Taxpayer E, a calendar year corporation, filed its 1981 return on March 15, 1982. On March 1, 1986, the taxpayer and the Department executed an extension agreement extending the time for assessment or refund on 1981 until September 15, 1986. The taxpayer files a sales factor option on August 1, 1986. The year 1981 as well as 1982 through 1985 are open and affected by the option.

(2) How and When the Option Is Made

To exercise the option for taxable years prior to 1986 the taxpayer shall:

(a) file a completed option form, Form 4B-OP (a copy of Form 4B-OP is included on page 37 of this bulletin), with the Supervisor, Corporation Office Audit Unit, Wisconsin Department of Revenue, P.O. Box 8906, Madison, WI 53708 along with an amended Wisconsin franchise or income tax return, Form 4X, for each prior year for which exercising this option requires a recomputation of the sales factor, and, if applicable,

(b) file a supplemental petition for redetermination with the Appellate Bureau, Wisconsin Department of Revenue, P.O. Box 8907, Madison, WI 53708 on contested assessments, refunds or refund claim denials not yet acted on.

In ascertaining that the option applies to all open prior years, the determination shall be made as of the date the completed option is filed with the Department of Revenue. The postmark date shall be the date filed for options mailed to the Department, and if not mailed the date received in any Department of Revenue office for options that are hand-delivered.

IV. QUESTIONS:

Questions concerning the computation of the sales factor should be addressed to:

Audit Technical Services
Wisconsin Department of Revenue
Post Office Box 8906
Madison, WI 53708

V. EXAMPLE:

ABC Corporation has its investment income-producing activity in Wisconsin and it computes its Wisconsin net income using the apportionment method under s. 71.07(2), Wis. Stats. For 1985 it has revenue from the following sources:

Sales:		
Into Wisconsin	$ 5,000,000	
Into nexus states	10,000,000	
From Wisconsin to nonnexus states	4,000,000	
From Wisconsin to U.S. Government	1,000,000	$20,000,000
Interest Income:		
From trade accounts receivable	$ 10,000	
From investments (unitary)	100,000	110,000
Dividend Income (Unitary):		
Qualified for deduction per 71.04(4)(a)	$ 200,000	
Qualified for deduction per 71.04(4)(b)	100,000	
Not qualified for deduction	50,000	350,000
Capital Gains:		
Sale of capital stock (unitary)		
$500,000 (proceeds)—$350,000 (cost)	$ 150,000	
Sale of business assets in Wisconsin		
$200,000 (proceeds)—$150,000 (net cost)	50,000	200,000
Royalties from Patents (Unitary)		50,000
Gross Rents:		
Wisconsin real property (business)	$ 50,000	
Wisconsin personal property (business)	20,000	
Non-Wisconsin personal property (business)	20,000	
Wisconsin real property (nonbusiness)	60,000	150,000
Gross Income		$20,860,000

ABC Corporation would compute its 1985 sales factor based on the *U.S. Steel* and *IBM* decisions as follows:

	Wisconsin/ Numerator	Total/ Denominator
Sales:		
Into Wisconsin	$5,000,000	$ 5,000,000
Into nexus states		10,000,000
Into nonnexus states (50% throwback)	2,000,000	4,000,000
To U.S. Government	1,000,000	1,000,000
Interest Income:		
From trade accounts receivable	10,000	10,000
From investments (unitary)	100,000	100,000
Dividend Income:		
$200,000 deductible per 71.04(4)(a) (100% deductible)	-0-	-0-
$100,000 deductible per 71.04(4)(b) (100% deductible*)	-0-	-0-
Other	50,000	50,000
Proceeds from Capital Gains:		
Sales of stock	500,000	500,000
Sale of business assets	200,000	200,000
Royalties from Patents (Unitary)	50,000	50,000
Gross Rents:		
Real property (business)	50,000	50,000
Personal property (business)	20,000	40,000
Real property (nonbusiness)	-0-	-0-
Total	$8,980,000	$21,000,000
Sales Factor Percentage to Wisconsin	42.7619%	

*50% deductible for taxable years 1980 through 1983 and 75% deductible for taxable year 1984.

If ABC exercised its option to compute its 1985 sales factor under the provisions of 1985 Wisconsin Act 120, its computation would be as follows:

	Wisconsin/ Numerator	Total/ Denominator
Sales:		
Into Wisconsin	$5,000,000	$ 5,000,000
Into nexus states		10,000,000
Into nonnexus states (50% throwback)	2,000,000	4,000,000
To U.S. Government	1,000,000	1,000,000
Interest Income:		
From trade accounts receivable	10,000	10,000
From investments (unitary)	-0-	-0-
Dividend Income:		
$200,000 deductible per 71.04(4)(a) (100% deductible)	-0-	-0-
$100,000 deductible per 71.04(4)(b) (100% deductible*)	-0-	-0-
Other	-0-	-0-
Proceeds from Capital Gains:		
Sales of stock	-0-	-0-
Sale of business assets	-0-	-0-
Royalties from Patents (Unitary)	50,000	50,000
Gross Rents:		
Real property (business)	50,000	50,000
Personal property (business)	20,000	40,000
Real property (nonbusiness)	-0-	-0-
Total	$8,130,000	$20,150,000
Sales Factor Percentage to Wisconsin	40.3474%	

*50% deductible for taxable years 1980 through 1983 and 75% deductible for taxable year 1984.

2. Deductibility of Motor Carriers' Operating Authorities

Statutes: section 71.04(8), 1983 Wis. Stats.

Note: This Tax Release, which was published in *Wisconsin Tax Bulletin* #32 dated April 1983, has been withdrawn. In *Star Line Trucking Corporation vs. Wisconsin Department of Revenue*, Docket No. I-10609, September 23, 1985, the Wisconsin Tax Appeals Commission concluded that 1980 was the proper tax year in which the taxpayer may write off the value of its motor carrier interstate operating rights. See the summary of the *Star Line Trucking Corporation* decision in the "Report on Litigation" in this bulletin.

3. Bad Debts - Savings and Loan Associations

Statutes: sections 71.04(7) and (9)(b), 1983 Wis. Stats.

Facts and Question: The Wisconsin Tax Appeals Commission decision in *Liberty Savings and Loan Association vs. Department of Revenue* (Docket No. I-6426, December 22, 1982) concluded that a savings and loan association is allowed under s. 71.04(9)(b), as it applied to the years 1972 through 1976, a bad debt deduction for two-thirds of the amount actually transferred to its Federal Insurance Reserve (FIR) account if that amount is reasonable and within the federal and state requirements.

For years 1981 and thereafter, federally chartered savings and loans are no longer required by the Federal Home Loan Bank to make an allocation to a loss reserve. The statutory reserve is a net worth requirement determined by audit of an organization's undistributed earnings, bad debt reserve, capital stock (if a stock company) and other surplus reserves. A state chartered savings and loan insured by the FSLIC must still maintain the FIR account and make appropriate transfers to that account.

What is the allowable bad debt deduction under s. 71.04(7) or 71.04(9)(b), 1983 Wis. Stats., for Wisconsin corporation franchise or income tax purposes for a year in which no transfer was made to the book FIR account by a savings and loan association?

Answer: Since no transfers were actually made to the book FIR account, no deduction is allowable under s. 71.04(9)(b), 1983 Wis. Stats. However, in lieu thereof actual bad debts sustained during the year are allowed as a deduction under s. 71.04(7), 1983 Wis. Stats.

4. Nexus and Certain Exempt Activities for Foreign Corporations

Statutes: sections 71.01(1), (2) and (2m), 1983 Wis. Stats.

Wis. Adm. Code: section Tax 2.82, September 1983 Register

Note: This Tax Release applies only with respect to taxable years 1983 and thereafter.

Background: 1983 Wisconsin Act 89 amended sections 71.01(1) and (2), Wisconsin Statutes, and created section 71.01(2m), effective for the 1983 taxable year and thereafter, as follows:

> "(2m) ACTIVITIES THAT DO NOT CREATE NEXUS. A foreign corporation may do business, exercise its franchise and own property in this state to the limited extent referred to in the following activities, in addition to those activities permitted under P.L. 86-272, without subjecting itself to the imposition of the income or franchise tax under subs. (1) and (2):
>
> (a) The storage for any length of time in this state in or on property owned by a person other than the foreign corporation of its tangible personal property and the delivery of its tangible personal property to another person in this state when such storage and delivery is for fabricating, processing, manufacturing or printing by that other person in this state.
>
> (b) The storage for any length of time in this state in or on property owned by a person other than the foreign corporation, and the shipment or delivery outside this state by another person in this state, of the entire amount of the foreign corporation's tangible personal property fabricated, processed, manufactured or printed in this state.
>
> (c) If the foreign corporation is a publisher, the purchase from a printer of a printing service or of tangible personal property printed in this state for the publisher and the storage of the printed material for any length of time in this state in or on property owned by a person other than the publisher, whether or not the tangible personal property is subsequently resold or delivered in this state or shipped or delivered outside this state."

Facts and Question - Example 1: Company A is a U.S. corporation incorporated and domiciled in Ohio and doing business in all fifty states. A is a manufacturer and seller of pulp, paper and related products.

Company B is a U.S. corporation, incorporated in Delaware, domiciled in Ohio and doing business in Wisconsin. B, a wholly-owned subsidiary of A, is a seller of market pulp that is manufactured by various producers.

Company C, a foreign corporation, is incorporated and domiciled in Canada. C, a 50 percent-owned affiliate of A, is a manufacturer of pulp, paper and lumber.

C ships raw pulp from Canada, via common carrier, into Wisconsin for storage in a public warehouse. Such pulp remains in storage until sale. B, acting as C's representative, solicits customers for the purchase of the stored pulp and receives a commission for sales thereof. Upon consummation of the sale, the pulp is shipped, via common carrier, to a customer's facility.

The raw pulp is sold by B to companies located both within and without Wisconsin. Approximately 30 percent of the shipments of the warehoused pulp are to companies located within Wisconsin. The remaining shipments are to companies located without Wisconsin. A portion of the out-of-state shipments are made to facilities owned by A. All such purchasers use the pulp to manufacture and fabricate paper and related products.

The sequence of events that result in a sale is as follows:

(1) C ships pulp to a public warehouse in Wisconsin.

(2) B sells such pulp as C's independent agent.

(3) The pulp is then shipped to customers located within and without Wisconsin.

(4) The pulp is used by these companies for further activities as described in s. 71.01(2m).

Is Company C's activity in Wisconsin protected by s. 71.01(2m), 1983 Wis. Stats., and thus exempt from Wisconsin's franchise/income tax law?

Answer: No. The ownership of the property must remain in the foreign corporation throughout its presence in Wisconsin to exempt the foreign corporation from filing. Section 71.01(2m), 1983 Wis. Stats., does not provide exemption to a foreign corporation when sales orders are filled from a stock of goods located in Wisconsin owned by that corporation unless the out-of-state owner is a publisher and the goods are materials printed in this state. Company C must file Wisconsin franchise/income tax returns.

Facts and Question - Example 2: Corporation P, a publisher incorporated and domiciled in New Jersey, stores printing supplies (paper, ink, etc.) at Wisconsin locations. It also stores printed materials (books, magazines, etc.) in or on Wisconsin property owned by a Wisconsin corporation which has printed these materials in Wisconsin for the publisher. These printed materials are subsequently sold to customers located both within and without Wisconsin.

Is Corporation P's activity in Wisconsin protected by s. 71.01(2m), 1983 Wis. Stats., and thus exempt from Wisconsin's franchise/income tax law?

Answer: Yes. But any other activity exceeding the limits of P.L. 86-272, such as maintaining its employes at the printer's Wisconsin business location for quality control purposes, will subject Corporation P to Wisconsin's franchise/income tax law.

Facts and Question - Example 3: Corporation X, a New York based manufacturing company, has raw materials stored in a public warehouse in Wisconsin. Corporation X has the raw materials shipped by common carrier to Corporation W, a Wisconsin subcontractor, to process these raw materials before shipping them to Corporation X for the purpose of being combined with other materials into Corporation X's finished product.

Is Corporation X's activity in Wisconsin protected by s. 71.01(2m), 1983 Wis. Stats., and thus exempt from Wisconsin's franchise/income tax law for 1983 and all subsequent years?

Answer: Yes. The storage of raw materials in Wisconsin in a public warehouse for delivery to a Wisconsin subcontractor for processing, storage and shipment out of Wisconsin are protected activities.

5. Wisconsin Tax Treatment of Deferred Income by Corporations

Statutes: section 71.11(8)(a), 1983 Wis. Stats.

Wis. Adm. Code: section Tax 2.16, September 1983 Register

Facts and Question: Section 71.11(8)(a), 1983 Wis. Stats., provides that the income and profits of a corporation for the income year shall be computed in accordance with the method of accounting regularly employed in keeping its books, but if no method has been employed or if the method does not clearly reflect income, the computation shall be made in a manner that does, in the opinion of the Department, clearly reflect the income.

It has been well established by court decisions that under the accrual basis of accounting, income is accruable when all events have taken place to give the taxpayer a right to receive the income. This is known as the "claim of right" doctrine. Similarly expenses or deductions are accruable when all events have taken place to fix the taxpayer's liability for payment and the amount of the liability can be determined. There is another principle established by court decisions to the effect that a taxpayer who receives cash for property or services and has unrestricted use of the funds so received, is taxable on such income in the year in which it is received. Under this principle, if an advance payment is received in one year for services or property to be delivered in the following year, the advanced payment is taxable in the year in which received. This principle is contrary, however, to good accounting theory which requires that income and the costs and expenses of producing such income must be reported in the same accounting period.

What is the Wisconsin tax treatment of various types of income deferred for book purposes in accordance with Generally Accepted Accounting Principles?

Answer:

A. Prepayments for Delivery of Merchandise at a Later Date

Advance billings or refundable deposits made in one accounting period for specific merchandise to be delivered in a subsequent accounting period may be deferred and reported as income in the year in which delivery of the merchandise is made to the customer. Income from the sale of merchandise on credit or the installment basis must be reported in full in the year in which the merchandise is delivered to the customer. Billings for tangible personal property delivered under a long-term supply contract are reportable as income in the year billed and may not be deferred until the contract has been completed. Prepaid subscription income may be reported ratably over the number of months covered by the subscription or may be reported in the year received, at the election of the taxpayer.

B. Advance Payments on Long-Term Construction Projects

Advance payments or progress payments under a general construction contract may, at the election of the taxpayer, be reported on the percentage of completion basis where costs can be matched against progress payments, or may be deferred and reported in the year in which the contract is completed.

C. Advance Payments for Future Services

Income from advanced ticket sales to a fixed schedule of events may be reported in the year received or prorated and included in the income in the year in which the events take place.

Advanced payments for personal services to be performed in a subsequent income year, for the right of occupancy or the exercise of any other right during a subsequent taxable year, are includible in income in the year received if the taxpayer has unrestricted use of the funds. This type of income may not be deferred even though there may be direct or indirect costs relating to the earning of such income in a subsequent tax year. See *Villa Maria, Inc. and Allen Hall Corp. vs. Wisconsin Department of Revenue*, Wisconsin Tax Appeals Commission, Docket Nos. I-2395 and I-2396, June 16, 1969 and *Commonwealth Land Title Insurance Co. vs. Wisconsin Department of Revenue*, Wis-

consin Circuit Court, Milwaukee County, No. 405-664, January 25, 1974.

Example: ABC Corporation sells and services office business machines. In this respect, it sells maintenance contracts for a fixed period of time. For book purposes this income is deferred and allocated to income over the period of the contract. However, for Wisconsin corporate franchise/income tax purposes the ABC Corporation must report this income when received since it has the unrestricted use of the funds. The difference in accounting for this income for book and tax purposes is summarized as follows:

	Per Books		Per Tax	
Item	1984	1985	1984	1985
Cash Received on Contracts	$ 100,000	$ 150,000	$100,000	$150,000
Deferred to Period Earned	(15,000)	(25,000)	-0-	-0-
Income from Deferred	-0-	15,000	-0-	-0-
Income Reported	$ 85,000	$ 140,000	$100,000	$150,000

The above methods of accounting for prepayments are considered to clearly reflect income for Wisconsin taxpayers under s. 71.11(8)(a), 1983 Wis. Stats. Therefore, a change in such methods of accounting for Wisconsin tax purposes may not be made without first obtaining Department approval under Wis. Adm. Code section Tax 2.16.

6. Doctrine of Recoupment in Pending Cases Where Taxpayer Has Paid an Admitted Portion of Tax

Statutes: section 71.12(1)(b), 1983 Wis. Stats.

Background: The case *American Motors Corporation v. Department of Revenue*, 64 Wis. 2d 227, 219 N.W. 2d 300 (1974), stands for the proposition that either the state or the taxpayer can counter with a "stale" claim (i.e., a claim barred by the statute of limitations) to the extent of an additional assessment or refund, so long as the same year or income tax period is involved.

Section 71.12(1)(b), Wis. Stats., provides in part, "A person may also pay any portion of an assessment which is admitted to be correct and the payment shall be considered an admission of the validity of that portion of the assessment and may not be recovered in an appeal or any other action or proceeding."

Question: In light of the above cited section of the law, can the Department issue a refund or permit an offset from an admitted payment?

Answer: No, once an additional assessment is admitted and paid after a petition for redetermination has been filed regarding the additional assessment, the admitted additional assessment cannot be subsequently recovered.

The following examples clarify how *American Motors* and s. 71.12(1)(b), Wis. Stats., would apply in various situations:

Example 1

Facts: The Department issues an additional assessment based on two points.

The taxpayer contests only the first point and admits and pays the remainder of the additional assessment.

The taxpayer later decides that he wants to contest the second point.

Outcome: Regardless of whether the taxpayer wins or loses on the first point, he cannot seek recoupment or contest the second point. Per s. 71.12(1)(b), Wis. Stats., the second point was admitted and paid and, therefore, not recoverable in an appeal or any other action or proceeding.

According to the language of s. 71.12(1)(b), Wis. Stats., the admission takes place at the time of payment, thus even in cases held in abeyance by the Department pending the outcome of another case, the taxpayer is barred from amending his petition for redetermination to contest the second point after the additional assessment on the second point is admitted and paid.

Because s. 71.12(1)(b), Wis. Stats., provides that the admission barring future recovery occurs at the time of payment, the doctrine of recoupment would be available to the taxpayer until the taxpayer pays the admitted portion of the assessment.

Example 2

Facts: The Department of Revenue issues an additional assessment based on two points.

The taxpayer contests the first point and admits and pays the remainder of the additional assessment.

The taxpayer later discovers a new basis for a claim for refund based on the same tax year or period. The claim for refund is now barred by the statute of limitations (i.e., it is a "stale" claim).

Outcome: If the taxpayer ultimately loses on the first issue and is required to pay the additional assessment, he is entitled to recoup the amount of the stale refund claim to the extent of the amount of contested additional assessment. The amount recoverable by the taxpayer cannot exceed the amount of the contested additional assessment.

If the taxpayer has not paid the admitted portion of the assessment, it would appear that the taxpayer can apply the doctrine of recoupment to the total additional assessment which has not been paid.

If the taxpayer ultimately wins on the first issue and is not required to pay the additional assessment, there is no assessment against which the taxpayer can assert his stale claim. Therefore, the stale claim is not recoverable.

Example 3

Facts: The Department of Revenue issues an additional assessment by office audit based on two points.

The taxpayer pays the total assessment and files for a refund on the first point before the expiration of the statute of limitations in s. 71.10(10)(e), Wis. Stats.

The refund is denied and taxpayer files a petition for redetermination, etc.

After the statute of limitations set forth in s. 71.10(10)(e), Wis. Stats., has expired, the taxpayer seeks a refund based on the second point.

Alternatively, the taxpayer seeks a second refund based on a totally new point arising out of the same tax year or

period after the statute of limitations set forth in s. 71.10(10)(bn), Wis. Stats., has expired.

Outcome: Regardless of whether the taxpayer wins or loses on the first refund claim, there is no assessment for the taxpayer to utilize for purposes of recouping his second stale refund claim. The taxpayer cannot increase the amount of his valid refund with stale refund claims. Therefore, the taxpayer's stale refund claims are barred.

Per *American Motors*, if the Department of Revenue has an additional assessment arising out of the same tax year or period which is closed to assessment by the statute of limitations, the Department of Revenue may recoup the additional assessment up to the amount of the refund if the taxpayer is successful. If the taxpayer does not ultimately prevail on its claim for refund, the Department of Revenue has nothing to offset its stale additional assessment against and, therefore cannot recover the stale assessment.

SALES/USE TAXES

1. Furnaces That May Be Used to Burn Bio-Mass Pellets or Lignite Fuel

Statutes: section 77.54(26m), 1983 Wis. Stats.

Facts and Question: A stoker-furnace has been specifically designed to produce heat by burning either lignite coal or bio-mass pellets. The primary use of the furnace is to provide forced-air central heating for a variety of types residential or light commercial installations.

Bio-mass pellets are not solid waste, but they are a product which has been produced from solid waste. For example, fuel pellets may be produced from solid waste, such as paper or cardboard.

Is the purchase of a furnace-stoker, which has been specifically designed to burn bio-mass (fuel) pellets produced from solid waste, exempt from the sales/use tax as waste reduction or recycling machinery and equipment under s. 77.54(26m), Wis. Stats.?

Answer: No. The exemption in s. 77.54(26m) does not apply to a furnace specifically designed to burn bio-mass pellets or lignite fuel as its primary purpose is to produce heat. The furnace does not recover energy from solid waste, but rather from a product of solid waste or from coal. This is the case even though the bio-mass pellets which are burned may have been produced in a recycling process. Waste reduction and recycling includes the process of taking solid waste and producing a new marketable product from solid waste, but it does not go beyond producing the new marketable product.

NEW WISCONSIN TAX LAWS

The Wisconsin Legislature enacted several changes to the Wisconsin tax laws in February, 1986. The following are brief descriptions of the major income, corporation franchise/income, sales/use, homestead, inheritance and excise tax provisions. All of the provisions described below are contained in 1985 Wisconsin Act 120, published February 7, 1986. The description for each item indicates the sections of the statutes affected and the effective date of the new provision.

INDEX

EXPLANATION OF TAX PROVISIONS OF 1985 WISCONSIN ACT 120

A. INCOME TAXES

1. Declaration of Estimated Tax Required for Estates and Trusts (Amend s. 71.21(title), (1), (2)(intro.), (3), (4), (6), (7) and (11), effective for 1987 taxable year and thereafter.)

Under prior law, estates and trusts were not required to make estimated tax payments. Beginning with the 1987 taxable year, estates and trusts will be required to make estimated tax payments in the same manner as individuals are required to, with one exception. The exception is that estates will not be required to make estimated tax payments for their initial taxable year.

B. CORPORATION FRANCHISE/INCOME TAXES

1. Declaration of Estimated Tax by Corporation - Due Date Changed (Amend s. 71.22(2)(c), (3)(a), (b) and (c), create s. 71.22(10)(c)4, effective for 1986 taxable year and thereafter.)

The due date by which corporations are required to make the final (4th quarter) installment payment of estimated tax for 1986 and subsequent tax years is moved up by one month. The final installment payment will now be due on or before the fifteenth day of the twelfth month of the income year. Under prior law, this payment was not due until the fifteenth day of the first month following the end of the income year. For example, a corpora-

tion with a calendar taxable year for 1986 will be required to make its final installment payment of 1986 estimated tax on December 15, 1986, rather than January 15, 1987, as prior law would have provided.

The exception to the addition to the tax penalty which is based on annualized net income (this exception is commonly identified as exception 3) is changed to reflect the new earlier due date for the final installment payment. The minimum payment amount for the final installment period for purposes of this exception will be determined on the basis of annualized Wisconsin net income for the first 11 months of the taxable year.

2. Situs of Income, Apportionable Income and Sales Factor Changed (Repeal and recreate s. 71.07(1m), create s. 71.07(2)(cm) and (cr), amend s. 71.07(2)(d)1.)

a. Effective Dates

(1) Except as noted in (2) and (3) below, the repeal and recreation of s. 71.07(1m) and the creation of s. 71.07(2)(cm) and (cr), which relate to apportionable income and the definition of "sales" in the sales factor, apply to the 1986 taxable year and thereafter, or, at the taxpayer's option, to all taxable years prior to 1986 that are open to assessment or refund. (Note: If a taxpayer opts to use the provisions of s. 71.07(1m), (2)(cm) and (cr) in 1985 Wisconsin Act 120 for any year prior to the 1986 taxable year, it must use such provisions for *all* years prior to 1986 that are open to assessment or refund. A copy of Form 4B-OP, "Option to Compute Sales Factor Under 1985 Wisconsin Act 120 for Taxable Years Prior to 1986" is included on page 37 of this bulletin.)

(2) The repeal and recreation of s. 71.07(1m)(b)2, which relates to the inclusion of income, gain or loss from farms, mines and quarries in apportionable income, applies to the first taxable year after the 1981 taxable year that is open to assessment or refund, and to subsequent taxable years.

(3) The creation of s. 71.07(2)(cm)2, which relates to inclusion of gross receipts from the operation of farms, mines and quarries in the sales factor, applies to the first taxable year after the 1981 taxable year that is open to assessment or refund, and to subsequent taxable years.

(4) The amendment to s. 71.07(2)(d)1 relating to the definition of "financial organization" is effective for the 1986 taxable year and thereafter.

b. Corporations Engaged in Business Wholly Within Wisconsin (Repeal s. 71.01(1m) and create s. 71.07(1m)(a))

For corporations which are engaged in business wholly within Wisconsin, all income is subject to, or included in the measure of, the Wisconsin income or franchise tax. (Note: The term "all income" does not include income which a state is constitutionally barred from taxing or including in the measure of a franchise tax.)

c. Apportionable Income (Repeal s. 71.07(1m) and create s. 71.07(1m)(b))

For corporations which are engaged in business both within and without Wisconsin and are subject to apportionment, apportionable income includes all income or loss (other than nonapportionable income in Part d below) including, but not limited to, income, gain or loss from the following sources:

(1) Sale of inventory.

(2) Farms, mines and quarries.

(3) Sale of scrap and by-products.

(4) Commissions.

(5) Sale of real property or tangible personal property used in the production of business income.

(6) Royalties from intangible assets.

(7) Redemption of securities.

(8) Interest on trade accounts and trade notes receivable.

(9) Interest and dividends if the operations of the payer are unitary with those of the payee, or if those operations are not unitary but the investment activity from which that income is derived is an integral part of a unitary business and the payer and payee are neither affiliates nor related as parent company and subsidiary. In this subdivision, "investment activity" includes decision making relating to the purchase and sale of stocks and other securities, investing surplus funds and the management and record keeping associated with corporate investments, not including activities of a broker or other agent in maintaining an investment portfolio.

(10) Sale of intangible assets if the operations of the company in which the investment was made were unitary with those of the investing company, or if those operations were not unitary but the investment activity from which that gain or loss was derived is an integral part of a unitary business and the companies were neither affiliates nor related as parent company and subsidiary. In this paragraph, "investment activity" has the same meaning as under (9) above.

(11) Management fees.

(12) Franchise fees.

(13) Treble damages.

(14) A general partner's share of income or loss from a partnership.

(15) A limited partner's share of income or loss from a partnership if the investment activity from which that share of income or loss is derived is an integral part of a unitary business. In this paragraph, "investment activity" has the same meaning as under (9) above.

(16) Foreign exchange gain or loss.

(17) Sale of receivables.

(18) Rentals of, or royalties from, real property or tangible personal property if that real property or tangible personal property is used in the business.

(19) Sale or exchange of petroleum at the wellhead.

(20) Personal services performed by employes of the corporation.

(21) Patents, copyrights, trademarks, trade names, plans, specifications, blueprints, processes, techniques, formulas, designs, layouts, patterns, drawings, manuals and technical know-how.

(22) Redemption of the corporation's bonds.

(23) Interest on state and federal tax refunds on business income or business property.

d. Nonapportionable Income (Repeal s. 71.07(1m) and create s. 71.07(1m)(c))

Income, gain or loss from the following sources are nonapportionable and shall be allocated to the situs of the property:

(1) Sale of nonbusiness real property or nonbusiness tangible personal property.

(2) Rental of nonbusiness real property or nonbusiness tangible personal property.

(3) Royalties from nonbusiness real property or nonbusiness tangible personal property.

(Note: All income, gain or loss from intangible property that is earned by a personal holding company, as defined in section 542 of the Internal Revenue Code, as amended to December 31, 1974, shall be allocated to the residence of the taxpayer.)

e. Sales Factor (Create s. 71.07(2)(cm) and (cr))

Corporations subject to apportionment will continue to use a three-factor formula for determining the amount of net income to be apportioned to Wisconsin. The three factors include payroll, property and sales.

Section 71.07(2)(cm) which was created in 1985 Wisconsin Act 120, provides that for purposes of the sales factor in s. 71.07(2)(c), "sales" includes, but is not limited to, the following items related to the production of business income.

(1) Gross receipts from the sale of inventory.

(2) Gross receipts from the operation of farms, mines and quarries.

(3) Gross receipts from the sale of scrap or by-products.

(4) Gross commissions.

(5) Gross receipts from personal and other services.

(6) Gross rents from real property or tangible personal property.

(7) Interest on trade accounts and trade notes receivable.

(8) A general partner's share of the partnership's gross receipts.

(9) Gross management fees.

(10) Gross royalties from income-producing activities.

(11) Gross franchise fees from income-producing activities.

Section 71.07(2)(cr) provides that the following items are among those that are not included in "sales" for purposes of the sales factor in s. 71.07(2)(c).

(1) Gross receipts and gain or loss from the sale of tangible business assets, except those under s. 71.07(2)(cm) 1, 2 and 3.

(2) Gross receipts and gain or loss from the sale of nonbusiness real or tangible personal property.

(3) Gross rents and rental income or loss from real property or tangible personal property if that real property or tangible personal property is not used in the production of business income.

(4) Royalties from nonbusiness real property or nonbusiness tangible personal property.

(5) Proceeds and gain or loss from the redemption of securities.

(6) Interest, except interest under s. 71.07(2)(cm)7, and dividends.

(7) Gain or loss from the sale of intangible assets.

(8) Dividends deductible under s. 71.04(4).

(9) Gross receipts and gain or loss from the sale of securities.

(10) Proceeds and gain or loss from the sale of receivables.

(11) Refunds, rebates and recoveries of amounts previously expended or deducted.

(12) Other items not includable in apportionable income.

(13) Foreign exchange gain or loss.

(14) Royalties and income from passive investments in property listed in s. 71.07(1m)(b)21. (See item c.(21) above for a listing of these items.)

(15) A limited partner's share of income or loss from a partnership.

f. Financial Organization (Amend s. 71.07(2)(d)1)

The definition of "financial organization" in s. 71.07(2)(d)1 is amended to include brokerage houses and underwriters.

(Note: The income of financial organizations continues to be apportioned according to rules of the Department of Revenue, s. 71.07(2)(e).)

3. Clarify Deduction for Taxes for Corporations (Other than insurance companies, regulated investment companies and real estate investment trusts) (Amend s. 71.04(3), effective for 1986 taxable year and thereafter.)

The amendment to s. 71.04(3) clarifies that sales and use taxes paid on items required to be capitalized are not deductible. It also clarifies that taxes imposed by any state or the District of Columbia on or measured by *all or a portion* of net income, gross income, gross receipts or capital stock are not deductible. (The words "all or a portion" were added to s. 71.04(3).)

4. Clarify Reference to Renewable Energy Resource System (Amend s. 71.04(16)(a) and (d), effective February 8, 1986.)

This provision clarifies that references to various parts of s. 16.957, Wis. Stats., which are made in the statutes that provide the rapid write-off provisions for a renewable energy resource system are references to the provisions of s. 16.957 of the 1985 Wisconsin Statutes.

C. SALES/USE TAXES

1. County Sales Tax - Adopting or Repealing an Ordinance Changed (Amend s. 77.70, create nonstatutory section 3046(5g), effective February 8, 1986.)

Repealing an Ordinance

If a county adopts an ordinance to impose a county tax, any repeal of such ordinance shall be effective on the date designated in the repeal ordinance; however, a certified copy of the repeal ordinance must be delivered to the Secretary of Revenue at least 30 days before the effective date of the repeal. (Note: Under prior law, the repeal was effective on December 31 of the year of repeal and 60 days notice to the Secretary of Revenue was required.)

Adopting an Ordinance

For the 1986 calendar year only, a county may adopt an ordinance imposing county sales and use taxes beginning on July 1, 1986, if a certified copy of the ordinance is delivered to the Secretary of Revenue at least 90 days prior to July 1, 1986.

D. HOMESTEAD CREDIT

1. Homestead Credit Formula Changed (Amend s. 71.09(7)(grm)(intro.), create s. 71.09(7)(grn), effective for 1986 claims (filed in 1987) and subsequent years' claims.)

Claimants with household income of $7,600 (prior law was $7,400) or less will receive a credit equal to 80% of their property taxes accrued and/or rent constituting property taxes accrued. If household income is more than $7,600, the credit will be 80% of the amount by which property taxes and/or rent constituting property taxes accrued exceed 13.483% (prior law was 13.187%) of household income exceeding $7,600.

E. INHERITANCE TAX

1. Consent to Transfer Fee Increased to $5 (Amend s. 72.29(1)(b)2 and (2)(b)2, effective February 8, 1986.)

The fee for the issuance of the inheritance tax Consent to Transfer Property form is increased from $1.00 to $5.00.

F. EXCISE TAXES

1. Repeal Requirement for Liquor Tax Stamp (Create ss. 139.092, 139.094, 139.096 and 139.098, repeal and recreate s. 139.06(1), repeal ss. 125.57(9), 139.06(5) to (8), 139.061 and 139.25(1), amend ss. 125.07(1)(b)3(intro.), 125.11(1)(c), 139.05(2a), 139.06(title), 139.06(2)(b) and (c), 139.06(3) and (4), 139.08(1) and (4), 139.10(1), 139.11(2), 139.12, 139.18(2) and 139.25(2) to (6), effective July 1, 1986 and thereafter.)

Beginning July 1, 1986, intoxicating liquor will no longer require Wisconsin intoxicating liquor stamp indicia as proof of payment of Wisconsin's liquor tax. Persons liable for payment of intoxicating liquor tax shall pay the tax directly to the Department of Revenue four times annually on an estimated basis. The due dates of the estimated taxes and appropriate returns are February 15, May 15, August 15 and November 15. The estimated payment shall be based on the expected actual tax liability for the calendar quarter for which the payment is due. An administrative fee of 3 cents per gallon shall be paid along with the estimated tax liability.

All persons required to file a return and pay intoxicating liquor taxes shall first provide security in the amount, at the time and of the type required by the department, or enter into a surety bond with a corporate surety to secure payment of the tax. In addition, all persons who were liable for payment of liquor taxes in either of the fiscal years 1984-85 or 1985-86 shall maintain a deposit with the department equal to 20% of the estimated tax liability for fiscal year 1985-86 or an amount specified by the department. The deposit shall be returned to the persons liable for the tax in the form of a credit over a 4-year period beginning August 15, 1987.

The department shall audit the returns and correct them as appropriate. If additional tax is due, the department shall within 4 years after the return is filed assess the amount due along with interest and penalties. The taxpayer may appeal an assessment within 60 days after the mailing of the assessment.

All taxpayers will continue to file monthly information reports.

(Note: The new liquor tax provisions have no effect on current administrative policy, procedure and practice for taxes on wine.)