11.14 Exemption certificates (including resale certificates)-A
11.16 Common or contract carriers-A
11.27 Warranties-A
11.28 Gifts, advertising specialities, coupons, premiums and trading stamps-A
11.39 Manufacturing-A
11.41 Exemption of property consumed or destroyed in manufacturing-A
11.45 Sales by pharmacies and drug stores-A
11.49 Service stations and fuel oil dealers-A
11.65 Admissions-A
11.66 Communication and CATV services-A
11.80 Sales of ice-A
11.84 Aircraft-A
11.85 Boats, vessels and barges-A
11.88 Mobile homes-A
11.94 Wisconsin sales and taxable transportation charges-A
11.96 Interest rates-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

Erwin D. Russell (p. 3)
Sale of residence

Annette L. Turner (p. 4)
Taxation of Indians

Corporation Franchise/Income Taxes

Avon Products, Inc. (p. 4)
Petition for review

ITT Life Insurance Corporation (p. 4)
Privileged documents

Kohler Company, Kohler Company—Successor to Kohler International Ltd., Kohlerco DISC, Inc. and KIL DISC, Inc. (p. 4)
Domestic International Sales Corporation

Project Systems, Inc. (p. 5)
Apportionment—nexus

Savings League of Wisconsin, Ltd., Equitable Savings & Loan Association, Liberty Savings & Loan Association, and Marathon County Savings & Loan Association (p. 6)
Dividends and interest—taxable

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Artex Corporation (p. 6)
Construction contractors—grain bins

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Computer and data processing—programs

Irvin Kozlovsky (p. 8)
Water conditioners

Homestead Credit

Myrtle Berglin (p. 9)
Property taxes accrued—joint ownership

INDIVIDUAL INCOME TAXES

Sale of Residence. *Erwin D. Russell vs. Wisconsin Department of Revenue* (Wisconsin Tax Appeals Commission, January 30, 1987). The issue pending before the Tax Appeals Commission is whether the taxpayer is required to report 100% of the gain realized from the sale of the real estate located at 8725 North Greenvale Road, in Bayside, Wisconsin.

Erwin D. Russell filed with the department his 1981 Wisconsin resident individual income tax return and reported on Schedule D $30,381 as proceeds received from the sale of real estate located at 8725 North Greenvale Road in the Village of Bayside.

The taxpayer and Flo Ann Russell, a/k/a Flo Ann O'Rourke, were divorced in Milwaukee County on November 10, 1970, and their judgment of divorce was dated November 30, 1970. Flo Ann Russell occupied the house located at 8725 North Greenvale Road until approximately January 20, 1981. On January 20, 1981, the property was sold to Richard W. and Margaret A. Render. Flo Ann O'Rourke, f/n/a Flo Ann Russell, and her then husband, Leslie E. O'Rourke, executed on January 18, 1981 a quit claim deed to the property. In the quit claim deed, the property was represented to be homestead property. The quit claim deed was duly recorded in the Milwaukee County Register of Deeds office on January 22, 1981.

The total amount of net proceeds from the sale of the real estate located at 8725 North Greenvale Road was $84,532.65. A check for the net proceeds was issued jointly to the taxpayer and Flo Ann Russell, dated January 21, 1985.

Flo Ann Russell received $54,944.90 of the total amount of the proceeds from the sale of the real estate in question, which represents 75% of the gain realized less an adjustment of $8,454.59 which was made in order to reimburse the taxpayer for various expenses he incurred during the period from December 1, 1970 to January 20, 1981. The expenses were for payments of principal on the mortgage, sewer assessments, water assessments, and repairs and improvements to the property. The taxpayer received $29,587.75 of the net proceeds from the sale of the real estate, which represents 25% of the gain realized from the sale plus an adjustment of $8,454.59 which was made in order to reimburse the taxpayer for various expenses he incurred during the period from December 1, 1970 to January 20, 1981.

The Commission concluded that income realized on the sale of real estate in Wisconsin is properly assessable to the record title holder of the property. The taxpayer realized 100% of the capital gain on the 1981 sale of the real property and the department acted properly in assessing an income tax on 100% of the gain realized on the sale of the property.

The taxpayer has not appealed this decision.

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Taxation of Indians. *Wisconsin Department of Revenue vs. Annette L. Turner* (Circuit Court of Dane County, January 21, 1987). This matter is on an appeal from an order of the Wisconsin Tax Appeals Commission in which it determined that the State of Wisconsin does not have jurisdiction or authority to tax an enrolled member of the Oneida Tribe and a domiciliary of the Oneida Indian Reservation for income earned on active duty in the United States Army while stationed in Kansas.

Sergeant Annette L. Turner, an enrolled member of the Oneida Indian Tribe and a domiciliary of the Oneida Indian Reservation in Wisconsin, claims a refund for taxes paid to Wisconsin on income earned while on active duty with the United States Army stationed outside the State of Wisconsin and outside the Oneida Indian Reservation. Her only source of income was from this service.

The Circuit Court concluded that based on state and federal law, and the special protections accorded Indians, Sergeant Turner's military income, earned while she is stationed in Kansas, is protected from Wisconsin income taxation. Accordingly, it found the Wisconsin Tax Appeals Commission's application of the law to be reasonable, and not arbitrary or capricious, and affirmed their order.

The department has not appealed this decision.

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CORPORATION FRANCHISE/INCOME TAXES

Petition for review. *Avon Products, Inc. vs. Wisconsin Department of Revenue* (Circuit Court of Dane County, August 21, 1986). The Department of Revenue moved the Court to dismiss Avon Products, Inc.'s action for lack of subject matter jurisdiction. The department asserted that Avon Products, Inc., failed to comply with the statutory requirements for service, resulting in a lack of subject matter jurisdiction.

The resolution of the motion to dismiss depends upon the Court's interpretation of s. 227.16, Stats., dealing with proceedings for review of administrative decisions. More specifically, the Court must determine which agency must be served with the petition for review personally or by certified mail. Here, Avon served the Commission with the petition by regular mail, while serving the department personally or by certified mail. The situation is complicated by the fact that the Commission did not actually receive the petition for review within the thirty day time limit for review set by s. 227.16. Two questions must be answered in order to resolve this motion:

A. Does s. 227.16(1)(a), Wis. Stats., require that Avon Products, Inc., serve the Wisconsin Tax Appeals Commission within thirty days of its final decision via personal service or certified mail?

B. If Avon Products, Inc., was required to serve the Commission within thirty days of the final decision via personal service or certified mail, was its failure to do so reasonable because of ambiguous statutory language?

The Circuit Court concluded that s. 227.16(1)(a), Wis. Stats., directs that the Wisconsin Tax Appeals Commission must be served personally or by certified mail with a petition for review within the thirty day time limit. Avon Products, Inc.'s failure to comply with this requirement was unreasonable as the statutory language was not ambiguous. Therefore, because the Court lacked subject matter jurisdiction, the department's motion to dismiss was granted. Because the Court determined that Avon Products, Inc., failed to meet the service requirement which must be strictly adhered to, there was no reason to reach the issue of timeliness of the service via regular mail attempted by Avon Products, Inc.

The taxpayer has not appealed this decision.

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Privileged documents. *Wisconsin Department of Revenue vs. Wisconsin Tax Appeals Commission and ITT Life Insurance Corporation* (Circuit Court of Dane County, October 15, 1986). The initial question for resolution is whether a writ of prohibition is an appropriate remedy in this factual situation. Secondly, the Court must determine whether the documents in question are, in fact, privileged under either the attorney-client communications theory or the work product theory.

The Department of Revenue sought a writ of prohibition restraining the Wisconsin Tax Appeals Commission from enforcing its recent decision ordering the Department of Revenue to produce certain documents sought by ITT Life Insurance Corporation. The Department of Revenue contends that the documents in question are privileged documents falling into a protected status under the attorney-client privilege and the attorney work product privilege.

In order to support issuance of the writ, the department must show that the ordinary remedies, such as appeal, are inadequate. The department must also show that grave or extraordinary hardship will result if the writ does not issue.

The Circuit Court concluded that all of the documents in question fall within the attorney-client communications privilege and, thus, are protected from discovery by the opposing party. It is beyond the scope of the Commission's authority to order that the materials be released to ITT.

The Wisconsin Tax Appeals Commission ignored a clear duty to protect the documents in question from discovery by ITT. Because compliance with the Commission's order followed by an appeal carries with it inherent harm, the Court found such a remedy to be inadequate, causing irreparable harm to the department. For these reasons, the Writ of Prohibition **shall** issue. The Wisconsin Tax Appeals Commission is prohibited from enforcing its order dated September 5, 1986, with regard to the documents enumerated.

The taxpayer has not appealed this decision.

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Domestic International Sales Corporations. *Wisconsin Department of Revenue vs. Kohler Company, Kohler Company - Successor to Kohler International, Ltd., Kohlerco DISC, Inc. and KIL DISC, Inc.* (Circuit Court of Sheboygan County, January 20, 1987). This is a review brought on the petition of the Wisconsin Department of Revenue for review of the

Wisconsin Tax Appeals Commission's decision and order dated November 22, 1985. The decision and order modified the department's actions on the taxpayer's petitions for redetermination of franchise taxes due from the taxpayers.

Kohlerco DISC, Inc. and KIL DISC, Inc., were organized in 1974 as wholly-owned subsidiaries of Kohler Company and Kohler International, Ltd., respectively. In 1977 Kohler International merged into the Kohler Company, and both DISC's therefore became wholly-owned subsidiaries of the Kohler Company. All of the taxpayers are Wisconsin corporations with headquarters at Kohler, Wisconsin.

Kohlerco DISC, Inc. and KIL DISC, Inc. were typical commission agent DISC's having no employees, no tangible property, and only the minimal corporate substance and transactions necessary for Kohler Co. and KIL to obtain the DISC benefit of federal tax deferral. The DISC's 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 DISC's had separate books and records which were maintained by employees of Kohler Co.'s corporate accounting department. These consisted of journals and ledgers reflecting commissions paid by the parents to the DISC's 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 account receivables from the DISC export sales. The latter device permitted the DISC's to satisfy the requirement that at least 95% of their assets be held in qualified export assets. The DISC's had separate bank accounts but because all payments to the DISC's were immediately returned to the parents, 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 state Appellate Courts which have considered taxation of the earnings of DISC's have all found that states can tax the same. However, the cases are split as to whether the tax is to be allocated to the DISC or the parent corporation. The cases have held that state laws permitting such taxation are constitutional, do not discriminate against interstate and foreign commerce, and are not in violation of the Supremacy Clause of the U.S. Constitution.

The department relies on s. 71.11(7m), Wis. Stats., which provides in part that the Department of Revenue "...may... allocate gross income...if (it) determines that such...allocation is necessary..."

On the undisputed facts the Tax Appeals Commission reached the following conclusion: "Income is taxable to the one who earns it, and therefore, the income of the DISC's should be allocated to the parent corporations, Kohler Co. and KIL for purposes of determining Wisconsin franchise taxes on said income, in order to clearly reflect the income of these corporations."

The Circuit Court affirmed the Wisconsin Tax Appeals Commission's decision.

The department has not appealed this decision.

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Apportionment—nexus. *Project Systems, Inc. vs. Wisconsin Department of Revenue* (Wisconsin Tax Appeals Commission, February 13, 1987). The issue before the Commission is whether, during 1974 through 1979, the taxpayer was entitled to apportion its income for Wisconsin franchise tax purposes between Wisconsin and Michigan under s. 71.07(2), Stats., and related administrative rules.

The taxpayer is a wholly-owned subsidiary of Allis-Chalmers Corporation and is part of the unitary business of Allis-Chalmers Corporation. The taxpayer is a member of the Allis-Chalmers combined group in Kentucky, California, Oregon, North Dakota, and Idaho for state income/franchise tax purposes. It pays a minimum tax in Minnesota. For the years 1977 through 1979, the taxpayer paid taxes to Michigan based on apportionment factors of 90.17%, 89.43% and 94.86%, respectively.

The taxpayer is a professional service corporation. Its principal business activity is providing professional engineering services (e.g., detail design of a building, foundation design, "civil" engineering).

The taxpayer has no real or tangible personal property. In lieu of payroll, the taxpayer pays management and service fees to Allis-Chalmers Corporation for the personal services of Allis-Chalmers Corporation's employes, for performing the taxpayer's managerial and engineering services. The taxpayer had no payroll, and had no employes other than its corporate officers who were employes of Allis-Chalmers Corporation and on the payroll of Allis-Chalmers Corporation. In carrying out the contracts, the Allis-Chalmers employes were responsible to and under the direct supervision and control of the taxpayer. In carrying out the contracts, Allis-Chalmers employes held themselves out to customers as the taxpayer's employes. The taxpayer's customers believed that Allis-Chalmers employes were employes of the taxpayer.

The management and services fees the taxpayer pays to Allis-Chalmers Corporation are for services performed by Allis-Chalmers Corporation personnel in Wisconsin and at the various job sites in Michigan, Minnesota, and Texas. Over the period 1974 through 1979, aggregate fees were approximately 20% for management and 80% for engineering. Management services are performed nearly all in Wisconsin. Eighty percent of the engineering services were performed in West Allis with the remaining 20% of the engineering services performed on job sites outside of Wisconsin.

The taxpayer reported an apportionment percentage to no state other than Wisconsin except on its Michigan 1977 through 1979 returns. The Michigan percentage consists of a gross receipts factor.

In disallowing the apportionment, the department Audit Bureau explained as follows:

Disallow Apportionment

"In accordance with Wisconsin Administrative Code Tax 2.39 t/p [taxpayer] has no provisions for using the apportionment method for Wi Franchise Tax purposes. T/P has no property, payroll or cost of performance in rendering its engineering services. Consequently, all income realized

cannot be apportioned and must be reported to Wi, a state where t/p maintains its commercial domicile."

In its petition for redetermination the taxpayer gave the following reason in respect to the apportionment issue:

"The disallowance of apportionment was in error because Wis. Adm. Code Tax 2.39(2) allows this corporation to apportion income. It has income from business activity subject to taxation in other states. It performs a portion of its engineering services in the state in which the respective project is located. Tax 2.39(4) defines compensation to include fees paid to a selected corporation as consideration for the performance of personal services. This taxpayer utilized the personal services of Allis-Chalmers employees for a fee to render engineering services in the State of Michigan. Taxpayer also purchased and resold goods in the ordinary course of its business which were destined outside the State of Wisconsin. These should be apportioned under Tax 2.39(5)."

In denying the petition for redetermination, the department stated as follows:

"It is the Department's position that the corporation does not have nexus in any other state and therefore is not entitled to use the apportionment method of reporting."

The Commission concluded:

A. During the years 1974 through 1979, the taxpayer had "nexus" with the State of Michigan, within the meaning of s. Tax 2.82(1)(a), Wis. Adm. Code.

B. During the years 1974 through 1979, the taxpayer was "engaged in business within and without the state" within the meaning of s. 71.07(2), Stats., and "subject to taxation by this state and at least one other state," within the meaning of s. Tax 2.39(2), Wis. Adm. Code. Accordingly, the taxpayer was entitled to use the apportionment method in determining its income for Wisconsin franchise tax purposes if it had proper sales, payroll or property factors upon which it could do so.

C. During the years 1974 through 1979, the taxpayer had no property upon which an apportionment property factor could be determined. The taxpayer's payment of management or service fees to Allis-Chalmers was "compensation" for purposes of the "payroll factor" under s. 71.07(2)(b), Stats., and s. Tax 2.39(4), Wis. Adm. Code. However, the situs of such compensation was Wisconsin under s. 71.07(2)(b)4, Stats.

D. For the years 1974 through 1979, the "sales factor" for apportionment purposes is determinable under s. 71.07 (2)(c)3, Stats., and s. Tax 2.39(5)(f)5. b.(iii), Wis. Adm. Code. Under the administrative provision compensation has a Wisconsin situs under s. 71.07(2) (b)4, Stats., if the other state lacks jurisdiction to tax. Such is not the case here. The taxpayer's gross receipts for sales factor purposes under s. Tax 2.39 (5)(f)5.b.(iii), Wis. Adm. Code, are apportionable between Michigan and Wisconsin in the ratio of the Wisconsin compensation to total compensation, that is, Wisconsin plus Michigan. There is no evidence of record as to what those respective costs were.

The department's redetermination that the taxpayer had no nexus in Michigan during 1974 through 1979 is reversed. The taxpayer's income is apportionable.

The department has not appealed this decision.

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Dividends and interest—taxable. *Savings League of Wisconsin, Ltd., Equitable Savings & Loan Association, Liberty Savings & Loan Association and Marathon County Savings & Loan Association vs. Wisconsin Department of Revenue* (Circuit Court of Dane County, August 20, 1986). The sole issue raised is whether the corporate franchise tax imposed by s. 71.03(1)(c) and (d), Wis. Stats., violates 31 U.S.C. 742 and Art. VI (supremacy clause) and Art. I Section 8, C1. 2 (borrowing clause) of the U.S. Constitution, because it is really an income tax that invalidly includes interest and dividends on U.S. government obligations as net income for tax purposes.

The Wisconsin franchise law requires earning of the income in the previous year and the exercise of the privilege of doing business in the state in the current year before a corporate franchise tax is imposed.

The Court concluded that Wisconsin's franchise tax is not an income tax, and that the inclusion of interest and dividends on U.S. government obligations does not violate either the supremacy or the borrowing clause of the U.S. Constitution. Therefore, the Court granted summary judgment for the department and declared s. 71.03(1)(c) and (d), Wis. Stats., valid.

The taxpayers have appealed this decision to the Court of Appeals.

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SALES/USE TAXES

Construction contractors—grain bins. *Wisconsin Department of Revenue vs. Artex Corporation* (Court of Appeals, District IV, January 26, 1987). The department appeals from an order of the Circuit Court affirming the Wisconsin Tax Appeals Commission's determination that because the grain bins Artex Corporation (Artex) constructed are manufacturing property within the meaning of s. 77.54(6)(a), Stats., Artex was therefore entitled to a use tax exemption under that statute. See WTB 44 for a summary of the Circuit Court decision.

Artex is in the business of constructing feed processing plants and grain elevators. Between December 1979 and November 1981, Artex installed some machinery and equipment at the Dane County Farmers Union Cooperative (Cooperative) to expand its corn processing facility. The machinery and equipment consisted of an aeration tank and system which, for the purpose of this appeal, shall be referred to as the grain bins.

In 1982, the department issued a use tax assessment against Artex for the amount of $24,939.33, including interest, on the materials Artex purchased and used to construct the grain bins. Because these materials were from out-of-state manufacturers, Artex had paid no Wisconsin sales or use taxes on its purchases of these materials.

Artex contends, and the Commission and trial court agreed, that it is exempt from paying use taxes in this case because the property which is the subject of the as-