2.61 Building and loan dividends on installment shares received by corporations -R
2.63 Dividends accrued on stock-A
2.70 Gain or loss on capital assets of corporations; basis of determination-A
3.01 Rents paid by corporations-A
3.05 Profit-sharing distributions by corporations-A
3.07 Bonuses and retroactive wage adjustments paid by corporations-A
3.14 Losses from bad debts by corporations-A
3.17 Corporation losses, miscellaneous-A
3.35 Depletion, basis for allowance to corporations-A
3.36 Depletion of timber by corporations-A
3.43 Amortization of trademark or trade name expenditures—corporations-A
3.48 Research or experimental expenditures-A
3.52 Automobile expenses—corporations-R&R
3.83 Domestic international sales corporations (DISCs)-A

D. Rules Adopted in 1989 But Not Yet Effective

1.001 Definition-A
2.14 Aggregate of personal exemptions-A
2.16 Change in method of accounting for corporations-A
2.19 Installment method of accounting for corporations-A
2.20 Accounting for acceptance corporations, dealers in commercial paper, mortgage discount companies and small loan companies-A
2.21 Accounting for incorporated contractors-A
2.22 Accounting for incorporated dealers in securities-R&R
2.24 Accounting for incorporated retail merchants-A
2.25 Corporation accounting generally-A
2.26 "Last in, first out" method of inventorying for corporations-A
2.45 Apportionment in special cases-A
2.50 Apportionment of net business income of interstate public utilities-A
2.505 Apportionment of net business income of interstate professional sport clubs-A
2.53 Stock dividends and stock rights received by corporations-A
2.56 Insurance proceeds received by corporations-A
2.65 Interest received by corporations-A
2.72 Exchanges of property by corporations generally-A
2.721 Exchanges of property held for productive use or investment by corporations-A
2.83 Requirements for written elections as to recognition of gain in certain corporation liquidations-A
2.88 Interest rates-A
2.90 Withholding; wages-A
2.91 Withholding; fiscal year taxpayers-A
2.92 Withholding tax exemptions-A
2.93 Withholding from wages of a deceased employe and from death benefit payments-A
2.956 Historic structure and rehabilitation of nondepreciable historic property credits-NR
3.09 Exempt compensation of military personnel-A
3.098 Railroad retirement supplemental annuities-A
3.44 Organization and financing expenses—corporations-A
3.45 Bond premium, discount and expense—corporations-A
3.82 Evasion of tax through affiliated interests-A

E. Rules Adopted in 1989

11.10 Occasional sales-A (effective 5/1/89)

F. Emergency Rules

2.956 Historic structure and rehabilitation of nondepreciable historic property credits-NR (effective 12/28/88; expires 7/26/89)
3.095 Income tax status of interest and dividends from municipal, state, and federal obligations received by individuals and fiduciaries-A (effective 1/1/89; expires 9/28/89)

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 the Commission's decision).

The following decisions are included:

Individual Income Taxes

Corporation Franchise or Income Taxes

Sales/Use Taxes

INDIVIDUAL INCOME TAXES

Tax protestors. *Kenneth William Koch vs. Wisconsin Department of Revenue* (Circuit Court of LaCrosse County, January 17, 1989). In this case, the department had evidence that the taxpayer had received income during the years in question and that the taxpayer had incurred withholdings for tax purposes. On that basis the department concluded that the taxpayer was required to file tax returns for those years. The department requested that the taxpayer file tax returns for those years. The taxpayer's position is that federal reserve notes are tax-exempt federal obligations. The taxpayer failed to present any evidence to the Commission to support his position.

The Court found that the Commission's decision was not based on any erroneous interpretation or application of sec. 71.10 or sec. 71.11(4), Wis. Stats., that the Commission's decision was not erroneous in that wages are taxable as income under Wisconsin income tax law, and that the Commission's decision was not erroneous in that federal reserve notes are not exempt obligations of the United States and are taxable. The Court further found that the taxpayer's challenge is frivolous as a matter of law in that he knew, or should have known, that the action was without reasonable basis in law and could not be supported by a good faith argument for extension, modification, or reversal of existing law. Therefore, the decision of the Commission and order that the taxpayer pay the costs of this action and reasonable attorneys' fees incurred by the State of Wisconsin under the provisions of sec. 814.025 and sec. 814.04, Wis. Stats., was affirmed.

The taxpayer has not appealed this decision.

❑

Domicile. *Edwin F. and Nancy L. Prizer vs. Wisconsin Department of Revenue* (Wisconsin Tax Appeals Commission, January 26, 1989). The only issues in dispute are Mr. Prizer's domicile for the years 1985 and 1986 and the underpayment penalty for estimated taxes for those years. It is the department's position that the taxpayer was domiciled in Wisconsin for the years 1985 and 1986 and that all his income is properly taxable by Wisconsin for those years. It is the taxpayer's position that he was jointly domiciled in Illinois and Wisconsin in 1985 and 1986, and that one-half of his income is properly taxable by Wisconsin, and the other one-half of his income is properly taxable by Illinois.

The taxpayer and his wife purchased their Grafton, Wisconsin, home on September 30, 1983, and moved into the house in June 1984. The taxpayer leased a furnished apartment in Illinois from September 1984 through December 15, 1986. In December 1986, the taxpayer rented an unfurnished condominium in Des Plaines, Illinois. Other than the Grafton, Wisconsin, home, the taxpayer owned no real estate during the years under review, 1985 and 1986. During the years 1985 and 1986, the taxpayer estimates that he spent approximately 148 days each year in Wisconsin, 173 days each year in Illinois, and 44 days each year in states other than Wisconsin and Illinois.

From June 6, 1984, through 1986, the taxpayer was employed by Convenient Food Mart, Inc. of Rosemont, Illinois. The taxpayer had been employed in Wisconsin and rendered services in Wisconsin from November 1981 through March 1984. The taxpayer was living in St. Louis, Missouri, when he accepted employment in Milwaukee, Wisconsin, in November 1981. The taxpayer generally spent the weekdays in Milwaukee, but commuted to St. Louis most weekends. During this time, the taxpayer generally stayed at the Park East Hotel in Milwaukee during the weekdays. After the taxpayer acquired the Grafton, Wisconsin, property in September of 1983, he lived at the Grafton, Wisconsin, residence during the week, but still commuted to St. Louis most weekends.

In March 1984, the taxpayer resigned his employment in Milwaukee and returned to St. Louis. In June 1984, the taxpayer accepted employment in Rosemont, Illinois. Also in June 1984, the taxpayer sold his home in St. Louis and he and his wife moved to their home in Grafton, Wisconsin. From June 1984 until September 1984, the taxpayer commuted daily from Grafton, Wisconsin, to Rosemont, Illinois. On or about September 1984, the taxpayer acquired an apartment in Rosemont, Illinois, and commuted to Grafton, Wisconsin, most weekends and holidays.

During the years under review, the taxpayer had two checking accounts. One account had a Grafton, Wisconsin, address and one account had an Illinois address. The Wisconsin checking account was used to pay Wisconsin expenses and some Illinois expenses. The account was opened prior to 1985 and remained open for the period under review. The taxpayer also had an Illinois checking account during the same period. The Illinois checking account was used to pay some Illinois expenses and as a depository. The account was opened prior to 1985 and remained open for the period under review.

The taxpayer used his Grafton, Wisconsin, address for purposes of his various insurance policies. The taxpayer gave his employer both his Grafton, Wisconsin, address and his Illinois address. The taxpayer filed his federal income tax returns with the Grafton, Wisconsin, address, filed his Wisconsin income tax returns with the Grafton, Wisconsin, address, and filed Illinois income tax returns with his Grafton, Wisconsin, address. During the years under review, the taxpayer did not belong to any Wisconsin or Illinois clubs, churches, social or professional organizations, used his Illinois address for his investment accounts and stocks, and had no invest-

ment advisors or brokers. The taxpayer's will listed his address as Illinois.

During the years 1985 and 1986, the telephone and utility bills in the taxpayer's Grafton, Wisconsin, home were in his name, and telephone and utility bills were in his name at his Illinois residences. The taxpayer was not registered to vote in any state, held a Wisconsin driver's license in 1985 and part of 1986, and obtained an Illinois driver's license on October 22, 1986. The taxpayer's child never attended any Wisconsin schools. The taxpayer's wife spent most of her time in Grafton, Wisconsin, approximately 321 days a year. She spent approximately 30 days a year each year in Illinois and approximately 14 days a year elsewhere each year. The taxpayer was not estranged or otherwise separated from his wife during the years under review.

The Commission concluded that during the years 1985 and 1986, the taxpayer was domiciled in the state of Wisconsin. The taxpayer could have only one domicile at a given time and could not acquire a new domicile in Illinois until he had actually abandoned his old domicile in Wisconsin. The taxpayer did not abandon his Wisconsin domicile nor establish a new domicile in Illinois during the period under review.

The taxpayer has not appealed this decision.

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CORPORATION FRANCHISE OR INCOME TAXES

Appeals, petition for redetermination; interest — assessments 12%. *Brunswick Corporation v. Wisconsin Department of Revenue* (Wisconsin Tax Appeals Commission, March 17, 1988). It was reported in WTB 60, page 7, that the taxpayer had appealed the Commission's decision in part. This is an error. The taxpayer has appealed the entire decision.

❑

Interest income—imputed. *J. C. Penney Company, Inc. vs. Wisconsin Department of Revenue* (Wisconsin Tax Appeals Commission, April 25, 1989). The taxpayer is a Delaware corporation operating a national merchandising business by way of retail chain stores as well as a mail-order sales business. The taxpayer does business in Wisconsin and is subject to the Wisconsin corporate franchise tax.

J. C. Penney Properties, Inc. ("Properties") is, likewise, a Delaware corporation and one of the taxpayer's wholly owned subsidiaries. Properties' business is the acquisition of real estate including the construction, purchase, and improvement of buildings used by the taxpayer as department stores or warehouses. It operates throughout the United States and, like the taxpayer, does business in Wisconsin, and is subject to the Wisconsin corporate franchise tax.

The taxpayer also leases buildings for department store use from unrelated parties. Properties is the sole provider of the taxpayer's leased warehouses.

Since 1962, the taxpayer has advanced funds to Properties for use in the acquisition and/or construction of real estate to be leased to the taxpayer as stores or warehouses. The taxpayer included these advances on its balance sheets and in Wisconsin franchise tax returns, reported them as "investments." Properties included these amounts in its balance sheets and in its Wisconsin franchise tax returns as "loans from stockholder."

After field audit, the department issued a notice of amount due dated October 29, 1984, containing an assessment of additional franchise tax to the taxpayer for fiscal years ending "FYE" January 26, 1980, through January 30, 1982, in the total amount, including interest, of $390,522.12. The majority of the additional assessment was based on the department's determination that these advances and similar advances to other of the taxpayer's subsidiaries were interest-free loans. Uncharged interest income was imputed by the department on these advances from the taxpayer to Properties under sec. 71.11(7m), Wis. Stats. The department allocated additional income for each of the three fiscal years covered by audit derived from interest imputed to the loans. The department applied the average prime rate of interest for each of the three fiscal years to the average net receivables balance for the year to arrive at the amount of imputed interest. Rates used were 12% for FYE January 26, 1980, 13% for FYE January 31, 1981, and 18% for FYE January 30, 1982, to the outstanding balance of advances at each year's end, thus deriving additional income in amounts which the department then allocated to the taxpayer.

At the Commission hearing and in its brief, the taxpayer clarified that it has withdrawn its objections to the assessment, except as respects FYE January 30, 1982. For that year, the taxpayer continues to object to the rate of the interest imputed by the department and the department's failure to allow offset for rentals made by Properties to the taxpayer at a bargain rate. The taxpayer argues that the difference between actual rent charged and "market" rent should be used to offset under sec. 71.11(7m), Wis. Stats., the imputed interest, regardless of which rate is finally determined to be proper.

The taxpayer did not directly charge interest on funds advanced to Properties. Rather, the advances were repaid by an arrangement whereby a periodic "rent" was charged the taxpayer by Properties for the long-term lease of the stores and warehouses in question, but never actually collected by Properties or paid by the taxpayer. Instead, the rent was applied to systematically reduce the debt owed the taxpayer by Properties. The rent for each property was set at an amount which would amortize the debt attributable to that property (i.e. the cost of the property paid for by Properties with funds received from the taxpayer) over a period of about 30 years for retail stores or 50 years for warehouses together with interest at a rate equal to the taxpayer's quoted borrowing rate on its senior debentures for the calendar quarter preceding the lease of the store or warehouse.

These rental rates were stated as a formula in a lease entered into for each property by

the taxpayer and Properties. The rents were never paid, but bookkeeping entries were used to amortize the debt owed to the taxpayer by Properties over the term of the lease. Thus, as each monthly rent payment became due on a store or warehouse, the taxpayer would debit rent expense and credit a clearing account on its books which records the amount of debt owed the taxpayer by Properties. At the same time, Properties would debit the clearing account in its books recording the company's debt to the taxpayer and credit rent income. If a property were sold by Properties, the proceeds would be used to further reduce the clearing account. As of January 30, 1982, the net debt owed by Properties to the taxpayer under this arrangement totalled $437,795,780. This amount was used by the department to impute interest income to the taxpayer on its non-interest bearing advances to Properties.

Had Properties charged market rents on its store leases to the taxpayer, the total 1981 rents would have been 30% higher, or $64,430,440 rather than $49,561,877. The rents charged the taxpayer by Properties for warehouses were also below fair market rents. Actual rents charged for the warehouses for FYE January 30, 1982, totalled $10,991,168. Fair market rents for the warehouse properties would have been $14,972,463 and, thus, $3,981,295 or 36.2% more than the actual rents charged by Properties for such warehouses.

There were no written instruments governing the taxpayer's advances to Properties, nor were there written notes or mortgages related to them. There were no written documents establishing an obligation of Properties to repay the advances.

The Commission concluded that the department's allocation of additional income to the taxpayer for its FYE January 30, 1982, under sec. 71.11(7m), Wis. Stats., upon interest free loans made by the taxpayer to Properties, was necessary clearly to reflect the taxpayer's income. However, the amount of income determined was excessive in these respects:

A. The department used only 1981 interest rates, when it should have used the various interest rates obtained when the loans in question were made by the taxpayer to Properties.

B. The department used a prime rate of interest, when it should have used the federal safe haven interest rates promulgated under sec. 482, IRC.

C. The department failed to allow a setoff for a non-arm's length rents charged the taxpayer by Properties under a rental arrangement designed to reimburse the taxpayer for its advances of funds to Properties.

The taxpayer and the department have not appealed this decision.

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Statute of limitations—waivers. *Sta-Rite Industries, Inc. vs. Wisconsin Department of Revenue* (Wisconsin Tax Appeals Commission, March 23, 1989). The issue for the Commission to determine is whether the tax assessment statute of limitations begins running on the date of taxpayer's mailing of the tax return or the date of department's receipt of the return.

On June 15, 1979, the taxpayer mailed to the department, certified mail, return receipt requested, its 1978 franchise tax return. The department received the return on June 18, 1979. On June 17, 1983, the parties entered into an agreement extending the department's assessment period for 1978.

At issue is the validity of the assessment extension agreement. The taxpayer claims the agreement was invalid, because it wasn't executed before the 4-year statute of limitations had expired. In support, the taxpayer argues the 4-year period began running on June 15, 1979, the date it mailed the return, and ran out on June 15, 1983, 4 years later and 2 days before the extension agreement was executed. The department counter-argues the statute didn't begin to run until June 18, 1983, when the department received the return. Therefore, the department says the statute hadn't expired on June 17, 1983, the date on which the extension agreement was executed.

The question here, thus, turns on whether the date of taxpayer's mailing of a return is the legal equivalent of the date of filing for the purposes of computing the limitation period.

The Commission concluded that there is no question that the return was properly addressed, had proper postage and postmark, and was received within 5 days. The precise statutory question boils down to whether mailing is the legal equivalent of filing. The Commission held that the terms mailing and filing are not legally synonymous, at least for the purpose of computing when the assessment period begins to run. Therefore, the department's denial of the taxpayer's petition for redetermination was affirmed.

The taxpayer has appealed this decision to the Circuit Court.

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Business loss carryforward—mergers. *Wisconsin Department of Revenue v. The United States Shoe Corporation* (Circuit Court of Dane County, February 28, 1989). The issues are:

A. Whether the Commission erred in denying U.S. Shoe's motion for summary judgment based on a closing agreement as to tax years 1976 and 1977.

B. If it did not, did the Commission err in its interpretation of sec. 71.06(1), Wis. Stats. (1975-76), to permit U.S. Shoe to deduct against its income for 1976 and 1977 the net business losses of a corporation merged with it on the last day of its fiscal year 1975.

C. If it did not, did the Commission err by limiting this deduction to an offset against only the income earned by the "same trade or business" that generated the losses.

U.S. Shoe is an Ohio corporation which has been subject to the Wisconsin franchise tax since fiscal year 1975 and is engaged in the manufacture and sale of shoes in Wisconsin and elsewhere. The Freeman-Toor Corporation (Freeman-

Ohio) was an Ohio corporation engaged in the manufacture and sale of shoes in Wisconsin and elsewhere during the fiscal year ending July 31, 1975. Freeman-Ohio was a wholly-owned subsidiary of U.S. Shoe and on July 31, 1975, was merged under the laws of Ohio into U.S. Shoe. The Freeman-Toor Corporation (Freeman-Delaware) was a Delaware corporation engaged in the manufacture of shoes in Wisconsin and elsewhere prior to August 1, 1974. On July 31, 1974, Freeman-Delaware was a wholly-owned subsidiary of U.S. Shoe and, on that date, Freeman-Delaware and all of its wholly-owned subsidiaries were merged under the laws of Ohio into Freeman-Ohio.

On its Wisconsin franchise tax return for the fiscal year ending July 31, 1976, U.S. Shoe claimed a net business loss offset of $899,594 based on the loss amount reported on Freeman-Ohio's 1975 Wisconsin return. Not all of the loss offset was used in fiscal 1976 so that on its return for the fiscal year ending July 31, 1977, U.S. Shoe carried forward and applied the excess as a fiscal 1977 offset of $139,926.

The department's March 7, 1980, assessment disallowed the claimed offset on the grounds that Wisconsin law does not permit a corporation, formed through merger, to offset against its income the losses of its predecessor corporations. The Commission reversed the department, concluding that U.S. Shoe was entitled to carry forward the losses of Freeman-Delaware or Freeman-Ohio during 1975 through 1975 as offsets against U.S. Shoe's 1976 and 1977 Wisconsin income for corporate franchise tax purposes under sec. 71.06(1), Wis. Stats. (1975-76). The March 7, 1980, assessment was also addressed to fiscal year 1978.

The Commission concluded that the changes in the statute were substantive, substantial, and material. On this basis, it concluded that *Fall River Canning* "is no longer operative." In doing so, the Commission found the new statutory language to be unambiguous and concluded that U.S. Shoe could deduct prior year losses of corporations with which it had merged as loss carryforwards under sec. 71.06(1), Wis. Stats.

On June 19, 1984, the department issued an assessment directed to fiscal years 1978 through 1983. U.S. Shoe and the department entered into a closing agreement on December 21, 1984. U.S. Shoe argued that this agreement foreclosed all efforts of the department to assess any further franchise taxes against it for any period before January 31, 1983. The Commission agreed insofar as fiscal year 1978, but not as to 1976 and 1977.

U.S. Shoe argues that the language of the final paragraph of the closing agreement is a separate undertaking between the parties and that, by its express terms, that paragraph unambiguously settles in final fashion its franchise tax liability for all years prior to January 31, 1983. In the alternative, it argues that the agreement is ambiguous and any ambiguity must be resolved against its drafter, here the department, to reach the same result.

The Court concluded that:

A. Taken in isolation, the final paragraph of the closing agreement would appear to lead to the conclusion urged by U.S. Shoe. The title of the agreement unequivocally specifies the period covered as "June 1, 1977, through January 31, 1983, inclusive." The first paragraph recites "that for purposes of settlement, the correct adjusted incomes . . . for the years July 31, 1978, to January 31, 1983, both inclusive, are . . . ." The attached schedules show calculations for six consecutive tax periods beginning with the fiscal year commencing on June 1, 1977, and ending on July 31, 1978, through the fiscal year ending on January 31, 1983. Further, the title to the agreement references the assessment of June 19, 1984, which indisputably was a field audit assessment. The language of the final paragraph, "a final disposition of the taxpayer's franchise tax liability," when read in reference to these other parts and features of the agreement can only be construed to mean the franchise tax liabilities that are addressed by the agreement, i.e., those for the periods June 1, 1977, through January 31, 1983.

B. The resolution of the second issue rests upon the proper interpretation of sec. 71.06(1), Wis. Stats. (1977-78). Section 71.06, Wis. Stats., had been construed in 1958 by the Supreme Court in *Fall River Canning*. The legislature had amended the statute in 1965 and again in 1975. On both occasions, the purpose of the changes made were clearly stated. On neither occasion, was there any mention made of the Court's construction in *Fall River Canning*, much less any expression of intent to change it. It must be presumed that the legislature, acting with full knowledge of a judicial construction and at least twice thereafter specifically addressing the statute construed, would have either used explicit language in its changes or included as its stated purpose in some part of the drafting record the desire to allow deductibility in the post merger situation, if that was its intent. It did neither, and thus the court must presume there was no intent to change the *Fall River Canning* construction. Thus, the Court found no basis for construing sec. 71.06(1), Wis. Stats. (1977-78), as effecting the viability of *Fall River Canning's* application of the statutory deduction of business loss carryforwards to the post merger setting.

C. Since the prior business losses of Freeman-Ohio and Freeman-Delaware cannot be claimed as a deduction by U.S. Shoe, there is no need to address the third issue.

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

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Closing agreements. *W. R. Grace & Co. vs. Wisconsin Department of Revenue* (Wisconsin Tax Appeals Commission, March 23, 1989). The issues for the Commission to determine are:

A. Whether the assessment dated October 12, 1981, (hereinafter referred to as the 1975 RAR assessment) issued to the taxpayer is barred by the closing agreement dated October 17, 1985.

B. Whether the department, by its actions in the course of settling two related matters regarding the taxpayer, agreed to absolve the taxpayer for all its franchise tax liability for 1975.