11.86(6) LANDSCAPING SERVICES. Gross receipts from landscaping and lawn maintenance services are taxable. Except as provided in sub. (5)(a), landscaping and lawn maintenance services include:

a. Landscape planning and counseling.

b. Lawn and garden services, such as planting, mowing, spraying and fertilizing.

c. Shrub and tree services.

d. Spreading topsoil and installing sod or planting seed where trenches have been dug or sump pump, transmission and distribution lines have been buried in residential, business, commercial and industrial locations, cemeteries, golf courses, athletic fields, stadiums, parking lots and other areas and along highways, streets and walkways.

(**Note:** In addition, the example that followed sub. (6) is deleted.)

Report on Litigation

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

The following decisions are included:

Individual Income Taxes

Bad debts — nonbusiness
Randy S. and Shirley S. Albee (p. 9)

Refunds, claims for — statute of limitations
Kurt H. Van Engel (p. 9)

Corporation Franchise and Income Taxes

Apportionable income
Unitary business
Dividends — deductible dividends
Albany International Corp. (p. 10)

Apportionment — apportionable income defined
Hercules Incorporated (p. 10)

Insurance companies — addback of exempt or excluded interest and dividends received deduction
Heritage Mutual Insurance Company (p. 13)

Insurance companies — addback of exempt or excluded interest and dividends received deduction
Insurance companies — interest from United States government obligations
Insurance companies — loss carryovers
American Standard Ins. Co. of Wisconsin
American Family Mutual Ins. Co. (p. 14)

Manufacturer's sales tax credit
Wausau Paper Mills Company (p. 15)

Sales and Use Taxes

Estoppel
Spickler Enterprises, Ltd. (p. 16)

Landscaping
Straight Arrow Construction Co., Inc. (p. 16)

Transportation charges
Rhinelander Paper Company, Inc. (p. 17)

Transportation charges
Trierweiler Construction and Supply Co. Inc. (p. 18)

Drug Taxes

Drug tax — constitutionality
Darryl J. Hall (p. 19)

INDIVIDUAL INCOME TAXES

Bad debts – nonbusiness. *Randy S. and Shirley S. Albee vs. Wisconsin Department of Revenue* (Wisconsin Tax Appeals Commission, February 11, 1997). The issue in this case is whether the taxpayers' deductions for unpaid wages and commissions, unreimbursed business expenses, and interest qualify as nonbusiness bad debts.

In August 1989, Randy S. Albee ("the taxpayer") began working for Bayshore Technologies, Inc. ("BTI"), a company located in Clearwater, Florida. Shortly after he began working for BTI, BTI stopped paying wages to its employes. An official of BTI asked its employes to continue to work for BTI and promised them they would be paid when the company was able to pay them. The taxpayer was paid a weekly wage through early November 1989. The taxpayer agreed to continue working for BTI in exchange for BTI's promise to pay him for his services once BTI had the ability to make these payments.

In January 1990, BTI sent a letter to the taxpayer indicating that it had become insolvent and that it was terminating the employment of all employes who had worked for BTI without pay. The taxpayer wrote to BTI to demand $21,187.51 which he believed was due to him under his employment arrangement with BTI. This sum consisted of wages and guaranteed commissions ($10,142.82), up-front living expenses, relocation expenses, and employe business related expenses ($10,932.93), and interest on past due expenses ($111.76). The wages and guaranteed commissions represented employe compensation and were not reported as his income for any year. The up-front living expenses, relocation expenses, and employe business related expenses represented amounts the taxpayer expended during 1989 and for which he believed BTI was obligated to reimburse him.

The taxpayers listed $3,500 of the amounts claimed against BTI as capital losses on their 1990 income tax return and another $500 on their 1991 return. The department disallowed these capital losses for both 1990 and 1991.

The Commission concluded that the taxpayers' claimed deductions for unpaid wages and commissions are not deductible because these amounts were not reported in gross income, that the deductions for unreimbursed business expenses are not deductible because they were not deducted in the year in which they were incurred, and that the deduction for interest is not deductible because the underlying deductions upon which they are based are not deductible.

The taxpayers have not appealed this decision.

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

Refunds, claims for – statute of limitations. *Kurt H. Van Engel vs. Wisconsin Department of Revenue* (Wisconsin Tax Appeals Commission, April 24, 1997). The issue in this case is whether refunds claimed by the taxpayer on his late-filed 1988 and 1989 income tax returns should be allowed as an offset against an assessment covering his late-filed 1990, 1991, and 1992 returns. The 1988 and 1989 returns were filed after the statutory deadline for claiming refunds.

The taxpayer is a Milwaukee businessman. In 1988 he was notified that he was the target of a federal criminal investigation, and in 1991 he was indicted by the United States for federal tax crimes. These charges were subsequently resolved through the federal legal system.

When the taxpayer was notified that he was the target of a federal investigation, he believed he was confronted with a real hazard of self-incrimination if he timely filed additional income tax returns. Consequently, on the advice of counsel, he declined to file returns for a number of years, including Wisconsin returns for 1988 through 1992. During this time he made payments to the State of Wisconsin, which he estimated would cover his annual tax liability.

In March 1995, after the federal criminal proceedings had concluded, the taxpayer filed state income tax returns for 1988 through 1992, more than four years after the unextended due dates of his 1988 and 1989 tax returns. On his tax returns for 1988 through 1991, the taxpayer claimed refunds which he asked to be applied to his next year's tax; for 1992, he claimed a refund. The refunds have since been reduced in accordance with adjustments allowed by the department to the taxpayer's 1987 return.

In August 1995, the department notified the taxpayer that the claims for refund covering the years 1988 and 1989 were rejected, because the returns were filed more than four years after the original due date. There is nothing in the record indicating that the department conveyed to the taxpayer any notice that he

had some right to ask for a redetermination of its decision or to appeal to the Commission. The taxpayer did not file a petition for redetermination of the decision of August 1995.

Because it had disallowed the taxpayer's claims for refund for 1988 and 1989, the department made adjustments to his other returns. It subtracted the refund from 1989 from the taxpayer's tax payment for 1990. The department assessed additional taxes for 1990, 1991, and 1992 in a notice dated September 11, 1995. The department denied the taxpayer's petition for redetermination, and in July 1996 the taxpayer sent to the Commission a petition for review covering tax years 1988, 1989, 1990, 1991, and 1992. He asserted in the petition that "overpayment credits from 1988 and 1989 are in excess of the total tax, interest and penalty balance due.... We are requesting that these credits offset the balance due."

This matter presents questions arising out of the taxpayer's substantial overpayment of estimated taxes but serious delinquency in filing returns. He filed a petition for review of his returns for 1988, 1989, 1990, 1991, and 1992 before the Commission in July 1996. The department moved to dismiss, asserting that (1) the taxpayer failed to state a claim upon which relief could be granted, (2) the statute of limitations on refunds had expired, and (3) the determination on the 1988 and 1989 returns was final and conclusive because the taxpayer failed to timely appeal the determination to the Commission.

The Commission concluded that the taxpayer's refunds from 1988 and 1989, otherwise barred by the statute of limitations, may be applied as an offset against the additional assessment of income taxes for the period 1990 through 1992 under the doctrine of "equitable recoupment." The petition for review asks that "overpayment credits for 1988 and 1989 ... offset the balance due" on the assessment for the later period. This request fairly pleads the issue of "equitable recoupment."

The doctrine of equitable recoupment in tax cases is an exception to the legislative policy of barring claims for and against the government in tax matters by statutes of limitations. It is a defense which permits the taxpayer to offset the department's money claim on grounds of equity and justice. The Commission held that the taxpayer will get nothing back, but the department will get nothing more.

The department has appealed this decision to the Circuit Court.

CORPORATION FRANCHISE AND INCOME TAXES

Apportionable income; Unitary business; Dividends – deductible dividends. *Wisconsin Department of Revenue vs. Albany International Corp.* (Circuit Court for Dane County, March 25, 1997). Both the department and the taxpayer filed a petition for review of the May 23, 1994, decision by the Wisconsin Tax Appeals Commission. See *Wisconsin Tax Bulletin* 88 (July 1994), page 11, for a summary of the decision.

The department and the taxpayer reached a settlement of all claims relating to this case. They agreed to settle the remaining issues in this case based on the settlement involving the department and NCR Corporation.

Based on this information, the Circuit Court dismissed the case with prejudice and without costs on March 25, 1997.

Apportionment – apportionable income defined. *Hercules Incorporated vs. Wisconsin Department of Revenue* (Wisconsin Tax Appeals Commission, February 26, 1997). The issues presented in this case are as follows:

A. Did the department properly include in the taxpayer's apportionable income, pursuant to sec. 71.25(5)(a), Wis. Stats., the gain realized by the taxpayer on the sale of its 38.7% interest in Himont, Inc., in 1987?

B. Did the department properly include in the taxpayer's apportionable income, pursuant to sec. 71.25(5)(a), Wis. Stats., the interest received by the taxpayer from Himont, Inc., in 1986 and 1987 on the $70 million working capital note?

C. Did the department properly include in the taxpayer's apportionable income, pursuant to sec. 71.25(5)(a), Wis. Stats., the gain realized by the taxpayer on the sale of its 13% interest in Erbamont, N.V. in 1986?

D. Did the department's inclusion of these amounts of gain and interest in the taxpayer's apportionable income violate the Due Process and/or Commerce Clauses of the United States Constitution?

Hercules Incorporated, a Delaware corporation, had its corporate headquarters and principal place of business in Wilmington, Delaware. The taxpayer's operations, including management of its investment port-

folio, were managed from its offices in Delaware.

Prior to November 1, 1983, the taxpayer was in the business, among other businesses, of manufacturing and marketing polypropylene. The polypropylene manufacturing business was not a part of the taxpayer's operations conducted in Wisconsin.

Polypropylene is a thermoplastic that is used to manufacture a wide variety of products, including appliance parts, automobile components, fibers, housewares, and other consumer products, packaging, and textiles.

Prior to July 1984, the taxpayer's domestic operations were divided into 5 separate and distinct lines of business: (1) organics, (2) plastics, (3) aerospace and explosives, (4) water soluble products, and (5) other products. The polypropylene manufacturing business was part of the Plastics business until November 1, 1983.

After July 1984, the taxpayer was reorganized into 3 business segments:

(1) Hercules Specialty Chemicals Company,

(2) Hercules Aerospace Company, and

(3) Hercules Engineered Polymers Company.

The polypropylene manufacturing business was not included in any of these business segments.

The taxpayer's operations in Wisconsin consisted of one paper chemicals manufacturing plant in Milwaukee. That plant's 4 main products were Kymene, used in wet-strengthened tissues and toweling, and Aqualpel, Pexol, and Scripset, all used as sizing agents in chemicals for the paper industry. No polypropylene was used or manufactured at this plant. The taxpayer's operations in Wisconsin also include a sales office in Green Bay for the sale of paper industry chemicals.

On June 28, 1983, the taxpayer entered into a joint venture agreement with Montedison S.p.A., an Italian company and a major worldwide producer of polypropylene. Pursuant to this agreement, Himont was formed on November 1, 1983, to acquire the polypropylene businesses formerly owned by the taxpayer and Montedison. After the taxpayer divested itself in 1983 of its polypropylene business, it no longer had any facilities, personnel, or technology to engage in, nor did it engage in, the business of manufacturing or marketing polypropylene.

Himont

Himont is a Delaware corporation, with its principal place of business in Wilmington, Delaware. At all times it was a separate legal entity, with its own management and its own board of directors.

The taxpayer and Montedison each received 50% of the stock in Himont in return for the transfer of their respective polypropylene assets and technology. In addition to the Himont stock received by the taxpayer, Himont provided to the taxpayer a promissory note in the original principal amount of $70 million. This note was designed to equalize the relative value of the assets acquired by Himont from the taxpayer and Montedison, due to the fact that the value of the assets acquired from the taxpayer exceeded the value of the assets acquired from Montedison. The note was payable in 5 years at variable interest rates.

In 1986, the taxpayer received interest from Himont in accordance with the terms of the $70 million note. The interest received was deposited in the taxpayer's general corporate account.

When Himont was created, it contracted for certain administrative services from the taxpayer and from Montedison pursuant to a series of written agreements. The services the taxpayer provided to Himont included accounting, contracting, payroll, finance, and insurance services, among others. Services were performed from 1983 through 1991.

The taxpayer leased 33,000 square feet of office space to Himont at the taxpayer's headquarters in Wilmington, Delaware, beginning in 1983 through April 1988.

Himont and the taxpayer entered into a polypropylene supply agreement. For the fiscal years ending October 31, 1985, through October 31, 1988, the total dollar amounts of polypropylene the taxpayer purchased from Himont were less than 13% of Himont's total sales.

The taxpayer's and Himont's personnel did not participate in common profit-sharing or pension plans, nor did the taxpayer provide employe benefit programs for Himont. To the extent former employes of the taxpayer had accrued or vested benefits at the time Himont was created, those accrued assets, and the associated liabilities, were acquired by Himont from the taxpayer.

The employes of the taxpayer who were hired by Himont initially received the same salaries, including bonuses and incentives, benefits, seniority, and pension plan, from Himont that they had received from the taxpayer.

In February 1987, Himont sold approximately 22.6% of its stock at $28 per share in a public offering. Upon completion of the sale, the taxpayer and Montedison each owned approximately 38.7% of Himont's issued and outstanding stock.

Negotiations between the taxpayer and Montedison resulted in the sale to Montedison, in September 1987, of the taxpayer's 38.7% interest in Himont for $59.50 per share. The taxpayer realized a 1987 net capital gain from the sale of $1,338,501,966. The taxpayer used the proceeds from the sale as follows:

- 30.6% to construct a plant for the aerospace business,
- 35.6% to repurchase the taxpayer's own common stock, and
- 33.7% to pay the taxpayer's taxes.

The taxpayer and Himont were functionally integrated. They engaged in transactions which were not at arm's-length, including the sale by Himont of polypropylene to the taxpayer at a discount from market, the sale by the taxpayer to Himont *at cost* of a wide range of administrative services, and the rental of substantial space by the taxpayer to Himont, also at cost.

There was centralized management between the taxpayer and Himont. The taxpayer had a management role grounded in the taxpayer's operational expertise in the polypropylene business. The taxpayer had the authority to select, and dismiss if appropriate — in each case with the concurrence of Himont's board — Himont's president, who in turn selected other key Himont officials. The taxpayer also nominated Himont's vice presidents for financial accounting and administration and the head of Himont's North American operations. The taxpayer selected as Himont's first president the manager of the taxpayer's polypropylene business, who left the taxpayer to assume the position. The taxpayer selected 3 of the 6 members of Himont's board of directors until 1987, when it selected 3 of 11 members. The taxpayer also had the authority to select the chairman of Himont's board of directors, who was Himont's chief executive officer (CEO). In 1987, the taxpayer's just-retired CEO became CEO of Himont. At that same time, 3 new "outside" director positions were added to the board along with 2 new "inside" director positions. Himont's new CEO and Himont's president became the new "inside" directors. Thus, the taxpayer effectively controlled 5 of 11 members of Himont's board in 1987.

Montedison selected the vice chairman of Himont's board of directors and nominated Himont's vice presidents for business management and technology and the head of Himont's European operations as well as a key employe in the financial area.

There were economies of scale between the taxpayer and Himont, reflected in the taxpayer's agreement to purchase most of its polypropylene needs from Himont, which were substantial, and in the taxpayer's providing to Himont a variety of services and space, at cost, throughout the period under review.

The taxpayer's investment in Himont served an operational purpose by reducing the taxpayer's exposure to commodity petrochemicals "without sacrificing our commitment to the polypropylene market" and by giving the taxpayer "immediate entry into the European staple fibers market."

After Himont was formed, the taxpayer did not provide it with financing or guarantees to assist in obtaining financing, nor was there joint ownership or use of any trademarks, service marks, trade names, logos, or product designs.

On its 1985, 1986, and 1987 Wisconsin corporate tax returns, the taxpayer reported dividends received from Himont as apportionable to Wisconsin.

Erbamont

On June 30, 1983, in exchange for a 50% interest in Adria Labs, Incorporated, the taxpayer acquired from Montedison 8% of the stock of Erbamont N.V., a New York Stock Exchange listed company engaged in the international pharmaceutical and health care business.

In connection with the creation of Himont, the taxpayer acquired an additional 5% of Erbamont's stock from Montedison, resulting in the taxpayer's ownership of 13% of Erbamont's stock.

In March 1986, the taxpayer sold its 13% interest in Erbamont and realized a net capital gain of $70,892,163. The proceeds from the sale were deposited in the taxpayer's general corporate account.

The taxpayer's board of directors monitored its Erbamont stock holdings for performance. No functional integration, centralized management, or economies of scale existed between the taxpayer and Erbamont. Except for electing 1 or 2 of the 12 members of Erbamont's board of

directors, the taxpayer never participated in or controlled Erbamont's management. Erbamont had its own management team, none of whom were former employes of the taxpayer, and there were no business transactions or contracts between the taxpayer and Erbamont.

The taxpayer's ownership of Erbamont stock served an investment rather than an operational purpose.

The taxpayer did not include the capital gains from the sales of its interests in Erbamont and Himont in apportionable income in its 1986 and 1987 Wisconsin corporation tax returns, nor did it include the interest received from Himont in its 1986 return, but treated these items an nonapportionable, nonunitary nonbusiness income.

Conclusions of Law

The Commission reached the following conclusions:

A. Yes, the department properly included in the taxpayer's apportionable income, pursuant to sec. 71.25(5)(a), Wis. Stats., the gain realized by the taxpayer on the sale of its 38.7% interest in Himont, Inc., in 1987.

B. Yes, the department properly included in the taxpayer's apportionable income, pursuant to sec. 71.25(5)(a), Wis. Stats., the interest received by the taxpayer from Himont, Inc., in 1986 and 1987 on the $70 million working capital note.

C. No, the department did not properly include in the taxpayer's apportionable income, pursuant to sec. 71.25(5)(a), Wis. Stats., the gain realized by the taxpayer on the sale of its 13% interest in Erbamont, N.V. in 1986.

D. No, the department's inclusion of these amounts of gain and interest in the taxpayer's apportionable income did not violate the Due Process and/or Commerce Clauses of the United States Constitution.

The taxpayer has appealed this decision to the Circuit Court. The department has not appealed. □

Insurance companies – addback of exempt or excluded interest and dividends received deduction. *Wisconsin Department of Revenue vs. Heritage Mutual Insurance Company* (Court of Appeals, District II, February 12, 1997). The department appealed from a Circuit Court order affirming a decision of the Wisconsin Tax Appeals Commission granting the taxpayer's claims for a partial refund of taxes previously paid for the years 1987 and 1988. For summaries of the prior decisions, see *Wisconsin Tax Bulletins* 92 (July 1995), page 16, and 96 (April 1996), page 16.

The question in this case is whether Heritage Mutual Insurance Company (Heritage) took the proper deduction pursuant to sec. 71.45(2), Wis. Stats. (1987-88), when computing its Wisconsin taxable income. This statute requires an insurance company to "add back" certain interest and dividend income allowed as deductions under federal tax law.

The starting point for computing an insurer's net income for purposes of Wisconsin tax law is the insurer's federal taxable income. For federal purposes, the insurer must include investment income and underwriting income. However, federal law allows an insurer to deduct certain interest and dividend income when determining its federal taxable income. These deductions include the interest earned on any state or local bond and certain dividends received.

In addition, an insurer is allowed to exclude from underwriting income its "losses incurred." These losses included losses actually paid plus increases in the reserve for losses incurred but not yet paid. Prior to the Tax Reform Act of 1986, federal law did not place any limitation on this "losses incurred" deduction. However, the Tax Reform Act scaled back this deduction by 15% of the sum of the exempt interest income and the allowable dividend deductions.

During this time, Wisconsin tax law remained constant. Both before and after the Tax Reform Act, sec. 71.45(2), Wis. Stats. (1987-88), required a Wisconsin insurer to "add back" to its federal taxable income the interest and dividend deductions which it had taken for federal tax purposes.

The department contends that the proper amount of the "add back" was the full amount of the federal deduction as reported by Heritage on its original state returns. Heritage contends that the proper amount is 85% of the federal deduction pursuant to the Tax Reform Act.

The department further contends that allowing insurance companies to add back only 85% of their interest and dividend income will result in a windfall to insurance companies. The department's concern stems from the fact that a portion of the tax-exempt loss reserves is funded