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3. Recording

The Wisconsin Supreme Court, in *Mutual Federal v. Wisconsin Wire Works,*[102] upheld Mutual's enforcement of the "due on sale" clause which was invoked as a result of Wisconsin Wire's conveyance of mortgaged property to Megal Development without Mutual's consent.[103] Wisconsin Wire, however, argued that Mutual had constructive notice of the conveyance by virtue of the recordation of the land contract by Megal. In so claiming, Wisconsin Wire contended that because of the recording Mutual had notice but failed to exercise their contractual rights for two and one-half years causing Mutual's acceleration rights to lapse. The essence of this line of argument is that the subsequent recording of the land contract could effect the rights of Mutual, a prior encumbrancer, since recording is "notice to all the world." The Wisconsin Supreme Court, however, held that the effect of the recording statute was nearly the converse of Wisconsin Wire's position. As a result Mutual was not charged with notice of Megal's subsequent recordation but rather Mutual's recorded mortgage was considered notice to Megal, the land contract vendee, that it took the land subsequent to a mortgage.[104]

RICHARD A. STACK, JR.

TAXATION

I. PRIMARY JURISDICTION OF THE TAX APPEALS COMMISSION

The authority of the Wisconsin Tax Appeals Commission was examined and clarified in *Sawejka v. Morgan.*[1] Administrative review of Wisconsin tax matters, before 1969, was performed by the Board of Tax Appeals whose function was restricted solely to reviewing applications for abatement and claims for refund.[2] The Board's jurisdiction was later expanded to review "all questions of law and fact" arising out of determinations by the secretary of the

102. *See supra* n. 74.

103. *See supra* n. 84.

104. 58 Wis. 2d at 112, 205 N.W.2d at 770.

1. 56 Wis. 2d 70, 201 N.W.2d 528 (1972).

2. *Created by* Wis. Laws 1939, ch. 412, to perform quasi-judicial functions. WIS. STAT. § 73.01(6)(c), renumbered § 73.01(5)(c) by Wis. Laws 1969, ch 276, sec. 333; Kaukauna v. Department of Taxation, 250 Wis. 196, 26 N.W.2d 637 (1947).

Department of Revenue.[3] The Board and its successor, the Wisconsin Tax Appeals Commission, has been described as an independent tribunal exercising quasi-judicial functions.

The Department of Revenue, in *Sawejka*, applied a selective retail sales tax statute to the taxpayer's coin-machine business. Contending misconstruction and unconstitutional application of the statute, the taxpayer commenced a declaratory judgment action in circuit court under section 269.56(1),[4] in an attempt to bypass the Tax Appeals Commission proceedings. The Department demurred and the trial court agreed to a lack of subject matter jurisdiction.

On appeal the taxpayer argued (1) the circuit court had jurisdiction to entertain the action,[5] and (2) where no administrative action is yet begun, no exhaustion of administrative remedy is required.[6] The Wisconsin Supreme Court agreed with the taxpayer on both arguments but, by deciding against the taxpayer, indicated that the argument was not extended far enough.

The court's first premise was the determination that section 269.56 gives the circuit court *concurrent* jurisdiction with the Tax Appeals Commission to hear and determine all questions of law and fact arising under the tax laws of this state. By so holding, the court put to rest the idea that the Commission has exclusive jurisdiction.

The second step in the court's reasoning was to reiterate the often-encountered doctrine of exhaustion of administrative remedies. Where some administrative proceeding has been commenced but is as yet uncompleted, then a court with jurisdiction concurrent with the agency should, in its discretion, decline to exercise its jurisdiction in favor of the agency.[7] Since the taxpayer in this case did not originally seek review by the Commission, the rule did not bar the commencement of the action in circuit court.

The taxpayer lost because he failed to take into account the primary-jurisdiction doctrine.[8] As a corollary to the checks and

3. WIS. STAT. § 73.01(4)(a)(1939); Neu's Supply Line v. Department of Taxation, 39 Wis. 2d 584, 159 N.W.2d 742 (1968).

4. ". . . Courts of record within their respective jurisdictions shall have power to declare rights, status and other legal relations whether or not further relief is or could be claimed. . . ."

5. Appellant's Brief 5.

6. *Id.* at 9.

7. 56 Wis. 2d at 79, 201 N.W.2d at 533.

8. The doctrine was not touched upon at all in Appellant's Brief, and only casually mentioned in the brief submitted by the Attorney General, Respondent's Brief 9. The first

balances theory of government, the doctrine has developed to promote comity or proper relations between courts and administrative agencies. The rule applied in *Sawejka* may be formulated as follows: where (1) a court and an administrative agency have concurrent jurisdiction over the subject matter, and (2) no formal proceeding is as yet under way before the agency, then the question of who is to make the initial determination depends upon the nature of the issues involved. If exclusively factual issues falling within the expertise of the agency are involved, the agency should be the first to review the matter. On the other hand, if issues of law, such as statutory interpretation, are significant and a valid reason for the intervention of the court is shown, then the court should exercise its discretion to entertain the proceedings. Since no reasons for judicial intervention were argued in *Sawejka*, and since the court assumed that there exist many factual issues as to the application of the retail sales tax statute to the taxpayer's business operations, the court concluded that the Wisconsin Tax Appeals Commission should have been given preference.

Would the taxpayer's procedure of commencing a declaratory judgment action in circuit court have been upheld if an argument concerning the definition of specific words in the retail sales tax statute had been made? If the Department of Revenue's policy of uniformly and systematically applying the statute had been attacked? The legislature gave the Tax Appeals Commission the jurisdiction to review "all issues of law and fact."[9] Yet, the Wisconsin Supreme Court appears to be desirous of restricting, to some extent, the Commission's authority to "exclusively factual issues,"[10] while leaving the strictly legal issues for the courts. There is need for clarification of the specific types of cases or issues which will be permitted to bypass the Wisconsin Tax Appeals Commission proceedings.

The attorney in *Sawejka* included in his brief a general contention that the Department of Revenue's action violated the equal protection clause of the Fourteenth Amendment to the United

Wisconsin case to deal with the doctrine was Wisconsin Collectors Ass'n v. Thorp Fin. Corp., 32 Wis. 2d 36, 43-46, 145 N.W.2d 33, 36-37 (1966); and the doctrine was expanded on in State v. Dairyland Power Cooperative, 52 Wis. 2d 45, 55-56, 187 N.W.2d 878, 883 (1971); the latest word was in State ex rel. Terry v. Traeger, 60 Wis. 2d 490, 499-500, 241 N.W.2d 4, 9-10 (1973).

9. *Supra* note 3.

10. 56 Wis. 2d at 80, 201 N.W.2d at 533, *quoting* Wisconsin Collectors Ass'n v. Thorp Fin. Corp., 32 Wis. 2d 36, 44, 145 N.W.2d 33, 36-37 (1966).

States Constitution.[11] In addition to its being a substitute for a stronger, more specific attack on the action of a governmental agency, why was the equal protection argument entirely ignored by the Wisconsin Supreme Court?

II. EQUAL PROTECTION ATTACK ON WISCONSIN TAX STATUTES

In contrast with the declaratory judgment proceeding in *Sawejka*, the typical procedure for raising a constitutional issue was illustrated in *Simanco, Inc. v. Department of Revenue.*[12] The taxpayer paid the tax, filed a claim for refund, and upon denial of the claim by the Department a petition for review was filed with the Tax Appeals Commission. The Commission's order affirming the denial was appealed to the circuit court. The court's reversal in favor of the taxpayer led to the appeal to the Wisconsin Supreme Court. Unfortunately, the taxpayer's conformance with the expensive and time-consuming statutory procedures went unrewarded.

In 1965 Simanco, Inc. sold all its assets for cash to Allis-Chalmers, and, as a liquidating corporation under section 71.337(1),[13] theoretically recognized no state income tax at the corporate level. The cash received by Simanco was then distributed to its shareholders in redemption of their stock, resulting in a gain realized by the stockholders to the extent that the amount received exceeded their adjusted basis.

Wisconsin, of course, is desirous of taxing the stockholders' gain to the extent permitted under the Constitution. Stockholders that are Wisconsin residents are unquestionably subject to the state's taxing power. The problem in this case was that 37.6 per cent of the stockholders were not residents of Wisconsin, and, in the ordinary case a state does not have the jurisdiction to tax a gain in the hands of a nonresident stockholder. Nevertheless, Wisconsin's right to tax a gain of a corporation subject to its laws was utilized in the 1961 amendment to section 71.337(1)[14] to establish a formula permitting the state to collect taxes from the liquidating

11. Appellant's Brief 108-09.

12. 57 Wis. 2d 47, 203 N.W.2d 648 (1973).

13. General rule. If a corporation adopts a plan of complete liquidation, and within the 12-month period beginning on the date of the adoption of such plan, all of the assets of the corporation are distributed in complete liquidation, less assets retained to meet claims, then no gain or loss shall be recognized to such corporation from the sale or exchange by it of property within such 12-month period. *Created by* Wis. Laws 1955, ch. 571.

14. *Id.* ". . . to the extent that such gain or loss is participated in by Wisconsin resident shareholders." *Added by* Wis. Laws 1961, ch. 190.

corporation to the extent that nonresidents participate in the distribution. Simanco complied with the statute in its Wisconsin tax return, but then sued for a refund of the $263,598.39 paid on that part of the gain which Simanco had distributed to nonresidents.

Simanco argued that the 1961 amendment to section 71.337(1) classifies a corporation for taxation solely on the basis of its proportion of nonresident shareholders. Such a classification dependent upon the residency of shareholders was alleged to be unconstitutional as effecting a denial of equal protection to corporations. For example,

> [I]f corporation A has no nonresident shareholders, it would pay no corporate franchise or income taxes if it liquidates under the terms of sec. 71.337(1), Stats., while corporation B, with 25 percent of its stock owned by nonresidents, would pay tax on one fourth of its gain. Corporation C, with 75 percent of its stock owned by nonresidents, would pay tax on three fourths of such gain. If corporation D is entirely owned by nonresident shareholders, it would be required to pay tax on the entire amount of such gain.[15]

The Supreme Court responded to Simanco's sole contention with a lively display of attitude. Distinguishing between the state's regulatory measures under its police power and its ability to raise revenue or grant exemptions through tax statutes, the court indicated that the all-too-common equal protection attack on the latter would be doomed to failure except in the most unusual cases. The legislature was recognized as having, in areas of economic and fiscal regulation, broad power to make classifications in pursuit of reasonable state policies. The judiciary was told to abandon the task of reviewing the legislature's product unless "apparent misclassifications are gross indeed" or there is a "clear and demonstrated usurpation of power."[16] "[A]bsolute equality and complete congruity of the treatment of classifications is impossible and must be sacrificed in the interests of preserving the governmental function."[17] "[W]here a tax measure is involved, the presumption of constitutionality is strongest."[18] Thus, the burden on one asserting

15. 57 Wis. 2d at 53-54, 203 N.W.2d at 651, *quoting* the circuit court's opinion, Appellant's Brief Appendix 105, and the Respondent's Brief in Support of a Motion for Rehearing 4. Simanco, Inc., used the example to justify its claim that the statute was grossly unfair.

16. *Id.* at 55, 203 N.W.2d at 652. "This court has recognized that the equal protection clause, . . . is of little moment in determining the constitutionality of a state tax." *Id.*

17. *Id.* at 54, 203 N.W.2d at 652.

18. *Id.* The best argument that Simanco, Inc., appeared to have to rebut the presump-

the unconstitutionality of a properly enacted statute must be close to impossible. A challenger must show that the selection or classification is capricious or arbitrary and that it has no reasonable purpose or relationship to the facts or a justifiable and proper state policy.

After enunciating the stringent standard, it was an easy matter for the court to decide in favor of the statute. Since section 71.337(1) does not accord different treatment to foreign and domestic corporations, and since the impact of the tax falls equally on the resident and nonresident shareholders of the liquidating corporation, the court reasoned that the classification, which results in a tax proportional to the nonresident shareholders, is a reasonable implementation of a legislative policy based upon a proper public purpose.

Unsettling language is found where the court sanctions, as a reasonable legislative policy, the operation of the statute whereby a Wisconsin stockholder is obliged not only to have his distributive share reduced by the tax on the corporation's gain apportioned to out-of-state residents, but, in addition, he is taxed on his personal distribution. As a result, the impact of the tax does in fact fall heavier on the resident stockholders. Recognizing the difference in tax treatment, Chief Justice Hallows and Messrs. Justices Connor T. Hansen and Robert W. Hansen dissented on the ground that all persons similarly circumstanced must be treated alike. Nevertheless, the majority justified the unfair burden by the statement that "those who are bound to a state by the tie of residence are proper persons to bear an additional onus of the cost of its operations."[19]

Any improvement in the situation was left for the legislature. One solution suggested by the trial judge would be to tax the entire gain in the hands of the corporation while affording a tax credit to the individual Wisconsin resident. Another method might be to revise the formula of section 71.337(1) so that the total liquidating distribution to all shareholders is determined first, and the corporation's tax payment is then taken only from the gain apportioned to nonresidents leaving the Wisconsin shareholders' distributive share to come from before-tax money.

Simanco thus teaches that the use of an equal protection argument should be avoided except in the case of the state's use of its

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tion of constitutionality was "That presumption can, however, carry appellant only so far." Respondent's Brief 5, and Respondent's Brief in Support of a Motion for Rehearing 7.

19. *Id.* at 59, 203 N.W.2d at 654.

police powers. A due process argument might have better success, but it too was ignored in *Transamerica v. Department of Revenue, infra.* If equal protection is the only possible argument, the attack must be very specific; the legislative policies underlying the statute should be extensively analyzed and criticized, and the relationship and operation of the statute to the facts should be shown to be unreasonable.

III. Application of Internal Revenue Concepts to Wisconsin Taxation

Prior to 1965, income taxation in Wisconsin was determined by an entirely independent computation of gross income and allowable deductions. There was no reference to a federal base. In July of 1965, the Wisconsin Legislature enacted an income tax "simplification law"[20] which, in general, provided that Wisconsin taxable income of individuals, corporations, estates and trusts shall be determined on the basis of federal taxable income, adjusted for certain modifications. The differences between the federal and state jurisdictions to tax guaranteed that the "simplification law" would be fraught with complexities.

A. Prepayments of Wisconsin Income Taxes

Section 71.21(19)(a) provides that any wage earner may be entitled to be completely exempt from Wisconsin payroll withholding if, before the beginning of his taxable year, he files a declaration and pays 100 percent of the estimated tax. The objective was to provide cash basis taxpayers a method whereby they could telescope their deductions for federal tax purposes.

Taking advantage of the above statute, at the end of 1964 the taxpayer in *Trepte v. Department of Revenue*[21] paid 100 percent of his estimated 1965 tax, and, at the end of 1965 he paid his 1966 estimated tax. On his federal returns, the taxpayer deducted the prepayments in the year paid. The Wisconsin Department of Revenue challenged the 1965 Wisconsin return because the taxpayer, in addition to using federal taxable income (thereby including a deduction for the prepayment in 1965 of the estimated 1966 Wisconsin tax liability), deducted the prepayment made in 1964 for the estimated tax on 1965 income as a "transitional adjustment modification."

20. Wis. Laws 1965, ch. 163.
21. 56 Wis. 2d 81, 201 N.W.2d 567 (1972).

The issue concerned the proper year to deduct from Wisconsin income a tax prepayment made in 1964 applicable to 1965 income. The court held in favor of the taxpayer by deciding that 1965 was the proper year to take the deduction. However, the court's reasoning warrants a careful analysis.

To begin with, the court found no merit in the arguments raised in the taxpayer's brief. Disregarding any presumption of administrative regularity, and, not even mentioning the Department's contentions, the court permitted the taxpayer to win by raising the critical issue sua sponte.

In essence, the court reasoned (1) a federal deduction is permissible in computations of state income taxes only for the year when the federal deduction *should* have been taken, regardless of when actually deducted on the taxpayer's federal return, (2) for federal purposes, a tax payment may be deducted only in the year made, providing a liability exists for which a prepayment might be made, (3) since a liability did not exist for 1965 taxes until income was earned during 1965, the prepayments were merely deposits upon prospective tax liability which had not come into existence, therefore, a payment made in 1964 in anticipation of taxes on income earned in 1965 would not be a proper deduction under section 164 of the Internal Revenue Code, nor for Wisconsin income taxes, until 1965.

Restricted to the facts of the case, the court nicely reasoned a victory for the taxpayer. However, if stated broadly, the rule of the case is that a cash basis taxpayer may not take a deduction for Wisconsin income tax purposes until a definite liability therefor comes into existence. Such a rule appears to be a strange and tricky overlapping of the cash and accrual methods. Extension of the *Trepte* reasoning could cause unnecessary theoretical difficulties.

Trepte at least indicates that a taxpayer utilizing the procedure of section 71.21(19)(a) to become exempt from Wisconsin payroll withholding must not deduct the tax payment on his Wisconsin tax return until the year for which the tax applies. For example, a tax paid at the end of 1973, applicable to the calendar year 1974, must be used to offset the 1974 tax liability on the return due in April of 1975. For the federal return, if IRS follows the reasoning of *Trepte*, the purpose of section 71.21(19)(a) will have been completely frustrated.

B. *Income in Respect of a Decedent*

The facts of *Estate of Rogovin v. Department of Revenue*[22] are simple. An estate received a $45 dividend check and a $44,219.89 bonus check a few days after decedent's death. The estate filed its Wisconsin income tax return using its federal taxable income as the starting point for computing Wisconsin taxable income. After scrutinizing section 71.03(2)(a), relating to exclusions from gross income, the attorney for the estate subtracted the full amount of dividend and bonus, included in federal gross income, to arrive at Wisconsin taxable income.

Prior to 1968, section 71.03(2)(a) excluded all inheritances from gross income for state income tax purposes, including income in respect of a decedent. Effective January 1, 1968, the statute was amended[23] to read:

> (2) EXCLUSIONS. There shall be exempt from taxation under this chapter the following:
> (a) The value of property acquired by gift, bequest, devise or inheritance, but such exemption shall *not* exclude from gross income the *income* from such property, . . . Any amount included in the gross income of a *beneficiary* under subchapter J of the internal revenue code [which includes section 691 providing for taxation of income in respect of a decedent] shall be treated for purposes of this paragraph as a gift, bequest, devise or inheritance of *income* from property. (Emphasis added)

The attorney for the estate argued that section 71.03(2)(a) refers only to amounts included in the gross income "of a beneficiary." Since an "estate" is not a "beneficiary," the dividend and bonus received should be excluded.

The court had no difficulty deciding in favor of the estate. Section 71.02(2)(i) provides that "terms not otherwise defined, have the same meaning as in the internal revenue code." Because the Internal Revenue Code carefully distinguishes between an "estate" and a "beneficiary," the two terms cannot be synonomous. The final point in the court's reasoning is interesting. The court in effect said that legislative intent is irrelevant since "[l]egislative acts are to be construed '. . . from their own language, uninfluenced by what the persons introducing or preparing the bill actually intended to accomplish by it.' "[24]

22. 57 Wis. 2d 683, 205 N.W.2d 136 (1973).
23. Wis. Laws 1967, ch. 239.
24. 57 Wis. 2d at 689-90, 205 N.W.2d at 139, *quoting* A. O. Smith Corp. v. Department

Estate of Rogovin thus stands for the proposition that the occasional porous nature of Wisconsin tax statutes holds many rewards for the careful reader. Once an ambiguity is discovered, the court will disregard any arguments attempting to delve into legislative intent.

IV. APPORTIONMENT OF INCOME OF MULTISTATE OPERATIONS

Transamerica Financial Corp. v. Department of Revenue[25] involved statutory construction of the word "total" as meaning either "all" or "less than all." The case is worthy of note, not because of the law or the reasoning by which the case was decided, but rather because of the technical context in which it was set. The specific problem with which *Transamerica* dealt—the applicability of section 71.07(2)[26] to financial organizations—has been mooted by recent legislative change[27] and forthcoming regulations under the Wisconsin Administrative Code. Nevertheless, apportionment of income has been a current topic of many state legislatures, including Wisconsin's,[28] while only infrequently discussed in the legal literature.

A. Background

Wisconsin has the power to tax income derived or received *within* its borders. The state, in most cases, does not have the

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of Revenue, 43 Wis. 2d 420, 427, 168 N.W.2d 887, 890 (1969). In response to the Rogovin case the Wisconsin Legislature amended WIS. STAT. § 71.03(2)(a) to subject to Wisconsin income taxation any amount included in the gross income of a beneficiary, *estate, trust or any other person* under Subchapter J of the Internal Revenue Code. Wis. Laws 1973, ch. 90.

25. 56 Wis. 2d 57, 201 N.W.2d 552 (1972).

26. The lengthy statute deals with allocation and apportionment of income.

27. Wis. Laws 1971, ch. 125, sec. 373.

28. *Id.* constitutes an entire revamping of WIS. STAT. § 71.07(2), of which the most significant change was to eliminate the cost of manufacturing, etc., factor in favor of a payroll factor used in weighting the amount of income apportioned to Wisconsin. The changes bring Wisconsin's statute very close to the formulation used in the Multistate Tax Compact. *See* P-H STATE & LOCAL TAXES—ALL STATES UNIT ¶ 5010 *et seq.* Wis. Laws 1973, ch. 90, sec. 352, again changed the apportionment formula so that the sales factor is, in effect, doubled. *See generally,* Bartz & Byers, *Money Market Mishmash,* 47 TAXES 174 (1969) (rationale of apportionment as applied to financial organizations); Harriss, *State-Local Taxation,* 50 TAXES 232 (1972); Keesling & Warren, *California's Uniform Division of Income for Tax Purposes Act,* 15 U.C.L.A. L. REV. 156 & 655 (1967) (excellent exhaustive analysis); Stanley & Tunstall, *State and Local Taxation,* 15 WAYNE L. REV. 271 (1968); Teschner & Sorden, *A Review of Wisconsin Income Tax Case Law Since 1946,* 1955 WIS. L. REV. 254, 256-64; ____, *Interstate Taxation Bill Goes to House Floor,* 47 TAXES 400 (1969) (development of uniform federal law).

power to tax income derived or received *outside* of Wisconsin. A multistate corporation is one which generates revenue from operations situated within the borders of more than one state. Each state generally wants to claim a share of the total taxable income. Theoretically, only 100 percent of the total income should be taxed by the various states. However, because of different apportionment techniques it is possible for a corporation to be paying state taxes on substantially more than 100 percent of its total income. Constitutional protections are available but do not immunize interstate instrumentalities from paying a nondiscriminatory share of the local taxation, if such tax is "properly apportioned to local activities within the taxing state forming a sufficient nexus to support the same."[29]

To meet the test, states traditionally developed the concept of a "unitary" business.[30] If multistate operations within the state are not an integral part of a unitary business then the tax department may permit the company to allocate a portion of its income to each state on the basis of its own accounting records. But if operations *in* the state are dependent upon or contributory to the operations *outside* of the state, then the corporation is deemed a unitary business and is generally required to determine the amount of income attributable to each state by means of statutory apportionment formulas.

B. Determination of Nonapportionable Income or Loss, or, the Significance of State Jurisdiction Over the Source or Recipient of the Income: Only Income Without a Definite Situs or Residence Will be Apportioned

Unless the state has obtained jurisdiction over the property, or over the person of the taxpayer (as by local presence of an individual, incorporation by a domestic corporation, or qualification by a foreign corporation), liability for taxation will depend upon whether or not the taxpayer has created a nexus or tax link by minimal activity within the state.[31]

29. Note, *Constitutional Law—Taxation—Sufficient Nexus to Satisfy Due Process of Law*, 1962 WIS. L. REV. 378, 378-79. U.S. CONST. art. I, § 8, provides that the regulation of interstate commerce is a matter to be handled by Congress. Also, the Due Process Clause prevents a state from projecting its taxing power beyond its borders.

30. WIS. STAT. § 71.07(2)(1947). Kessling & Warren, *supra* note 28 at 163-64; Kessling & Warren, *The Unitary Concept in the Allocation of Income*, 12 HASTINGS L.J. 42 (1960); Miller, *State Income Taxation of Multiple Corporations and Multiple Business*, 49 TAXES 102 (1971).

31. H. HENN, LAW OF CORPORATIONS §§ 81, 99 (2d ed. 1970).

In computing Wisconsin income taxes for a multistate corporation, one of the initial steps is to determine the taxable situs of income. "Nonapportionable income" is that income which is assigned to a definite state, and, as a result, is not allocated among two or more states. There are two categories of nonapportionable items. Under section 71.07(1), income which follows the situs of the property includes that derived from rentals and royalties from real estate or tangible personal property, or from the operation of any farm, mine or quarry, or from the sale of real property or tangible personal property. Income which follows the residence of the recipient includes income from personal services, from professions of resident individuals, and from all other sources including land contracts, mortgages, stocks, bonds and securities or from the sale of similar intangible personal property.

For a corporation completing a Wisconsin tax return, the above items must be assigned to a state. The total nonapportionable income will be subtracted from net income. The resultant amount is the income which has its situs at the place where the corporation does business. Since the company's activities produce sufficient minimum contact with several states, or take advantage of benefits or protection conferred by several states, the income is subject to apportionment among such states according to a formula. Income assigned to Wisconsin will be added back near the end of the computations. Figure 1 illustrates the computations and relationship between net, nonapportionable and apportionable income.

C. The Transamerica Case

Transamerica Financial Corporation was engaged in the business of consumer credit and installment sale financing in Wisconsin and 16 other states. Its operation involved borrowing money at one rate of interest and then lending that money, together with its equity capital, at a higher rate.[32] Consequently, interest income and interest expense were the major factors in determining Transamerica's net income. Transamerica also derived dividend income from subsidiaries located entirely outside of Wisconsin. Since Transamerica's income was not all subject to taxation in Wisconsin, the apportionment formula came into effect. In issue was the

32. The obvious purpose of a statute such as sec. 71.07(2), requiring the offsetting of interest expense against interest and dividend income, is to prevent a corporation from operating on borrowed money while investing its own capital in tax-exempt securities and thus, in effect, gaining a double exemption. Appellant's Brief 7.

FIGURE 1
(based upon hypothetical data)

TOTAL NET INCOME for the Entire Multistate Business Operation	$10,000
LESS NET NONAPPORTIONABLE INCOME (subject to tax by only one state):	
—Follows residence of recipient:	
• *Income from dividends and interest less related expenses*	$500
• Net profits from disposal of intangible assets	600
—Follows situs of property:	
• Net rental and royalty income from tangible property	700
• Net profit from disposal of tangible assets	800
Total Income Subject to Tax by Only One State	2,600
EQUALS APPORTIONABLE INCOME (subject to tax by each state in which the corporation is "doing business"— theoretically follows the situs of the business)	$ 7,400
TIMES APPORTIONMENT PERCENTAGE (property factor + payroll factor + sales factor) ÷ 3	20%
EQUALS Apportionable Income Allocated to Wisconsin	$ 1,480
ADD Nonapportionable Income Allocated to Wisconsin	1,520
EQUALS Total Wisconsin Net Income Subject to Tax	$ 3,000
TIMES Wisconsin Tax Rates	($85 plus 4.5% of excess over $3,000)
EQUALS Wisconsin Tax Payable	$ 85

construction of a phrase in section 71.07(2) which affects the italicized portion of Figure 1, to wit: "the amount of interest and dividends deductible . . . shall be limited to the total interest and dividends received."

The objective of any multistate corporation would be to have as much of its income as possible labeled "nonapportionable," thereby making it taxable by only one state (for Transamerica, the state would probably be its principal place of business, California), and not subject to being apportioned to each state in which it does business. Transamerica argued for a literal reading of the phrase "total interest and dividends received" as meaning *all* dividends and interest whether apportionable or nonapportionable, thereby setting a high ceiling with respect to the amount of items which it may label "nonapportionable." Since almost all of Transamerica's income came from dividends and interest, its deduction for nonap-

portionable items would be as large as its income, leaving nothing to be apportioned to, and subject to tax in, Wisconsin.

The Department of Revenue attempted to uphold the interpretation that it had applied for over twenty-five years, that only nonapportionable items are to be considered in calculating the total of nonapportionable income.[33] In other words, "total interest and dividends received" should mean only nonapportionable dividends and interest. Since some of Transamerica's income resulted from business done in Wisconsin, the Department, feeling that some tax should be paid, argued that Transamerica's dividend and interest income was apportionable, therefore none should be deducted.

With the issue thus obfuscated, the court resolved the matter on principles of statutory construction. The statute as written was clear, and so the court gave the language its ordinary and accepted meaning by deciding that "total" means all, and not only part. Thus Transamerica escaped Wisconsin taxation. The statute as applied to a financial organization was ambiguous since it was obvious that a corporation with only incidental dividend and interest income was contemplated by the legislature. The court threw up its arms and stated,

> when the legislature does impose a tax, it must do so in clear and express language, with all ambiguity and doubt in the particular legislation being resolved against the one who seeks to impose the tax.[34]

The result of *Transamerica* was to transfer the issue of apportionment of income of a multistate financial corporation back to the legislature. Yet, by the time *Transamerica* was decided the legislature had already exempted financial organizations from the operation of section 71.07(2) and had made the income "apportioned pursuant to rules of the department of revenue."[35] The problem of drafting regulations whereby dividend and interest in-

33. Appellant's Brief 12. 7 Wis. Admin. Code, TAX § 2.43 (1932), provides: The expenses related to nonapportionable income must be deducted therefrom to determine the net nonapportionable income. In the case of dividends and interest received which follows the residence of the recipient, only the excess of the amounts received over the sum of interest paid and dividends deducted plus other related expenses can be considered as nonapportionable income. *See*, Comment, *Function and Effect of Wisconsin Department of Taxation Income Tax Rules*, 40 MARQ. L. REV. 414, 425 (1957).

34. 56 Wis. 2d at 64-65, 201 N.W.2d at 555.

35. *Supra* note 27; WIS. STAT. § 71.07(2)(d)(1), (e) (1971).

come of a multistate financial organization is constitutionally apportioned to the states in which the business is transacted and from which the income is derived is presently being considered by the Department. The extreme complexity of the task, as illustrated by *Transamerica,* is evident.

MARTIN J. GREGORCICH

TORTS

I. PRODUCTS LIABILITY

The Wisconsin Supreme Court with two major decisions this term, has continued a trend to expand the products liability field which began with its decision in *Dippel v. Sciano.*[1] The *Dippel* case adopted the rule of strict liability in tort as set forth in the Restatement (2d) of Torts, sec. 402A[2] stating that privity of contract should not be used to defeat a claim based on a defective product unreasonably dangerous to a nonprivity consumer. However, the court's decision in *Dippel* limited its holding to the black letter rule of the Restatement. The court reasoned that while the comments of the Restatement reporters may be helpful in construing the section, the comments were not adopted in order to allow the concept of strict liability to develop within the context of existing law in this state. The court was called upon this term to consider the applicability of strict liability in a suit by an injured bystander against the manufacturer of the allegedly defective product in the case of *Howes v. Hanson.*[3] In addition the court considered the liability of a component part maker and the method of apportioning damages among parties in the distributive chain of a product in *City of Franklin v. Badger Ford Truck Sales.*[4]

1. 37 Wis. 2d 443, 155 N.W.2d 55 (1967).

2. *Special Liability of Seller of Product for Physical Harm to User or Consumer*

(1) One who sells any product in a defective condition unreasonably dangerous to the user or consumer or to his property is subject to liability for physical harm thereby caused to the ultimate user or consumer, or to his property, if

(a) the seller is engaged in the business of selling such a product, and

(b) it is expected to and does reach the user or consumer without substantial change in the condition in which itis sold.

(2) The rule stated in Subsection (1) applies although

(a) The seller has exercised all possible care in the preparation and sale of his product, and

(b) the user or consumer has not bought the product from or entered into any contractual relation with the seller.

3. 56 Wis. 2d 247, 201 N.W.2d 825 (1972).

4. 58 Wis. 2d 641, 207 N.W.2d 866 (1973).