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Taxation and Trusts and Estates

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commencement of construction, making it originally effective as a blanket lien against the whole property, but that upon filing of the condominium declaration it became effective against the individual units within the meaning of the statute, with the result that each unit owner was liable only for a proportionate share.

The critical time, the court ruled, is the date of commencement of foreclosure proceedings and the filing of a lis pendens against the property. So long as the condominium declaration is filed before foreclosure proceedings are commenced, section 703.09 applies and each owner is liable only for his proportionate share. However, if the foreclosure is started before the declaration is filed, "the situation is frozen so that the subsequent recording of a declaration does not transform the blanket lien into a proportional lien on individual units."[37]

The court explained its ruling by saying that foreclosure is an equitable proceeding and it is patently inequitable to charge individual unit owners with liability for the full value of a lien against the entire property.

MARY F. WYANT

TAXATION AND TRUSTS AND ESTATES

I. ACCRUED LIABILITIES

In Wisconsin, corporations are allowed to deduct from their gross income compensation paid to employees for services rendered.[1] Frequently, in addition to the employees' regular wages, companies will also pay bonuses and vacation pay, or both. When these payments have been made in good faith, and as additional compensation, they are likewise deductible.[2] *Ladish Co. v. Department of Revenue*[3] involved a situation where an accrual basis calendar year corporation was denied a

37. 73 Wis. 2d at 115, 242 N.W.2d at 898.

1. WIS. STAT. § 71.04(1)(1973).
2. Treas. Reg. § 1.162-9 (1958); McCoy-Brandt Mach. Co., 8 B.T.A. 909 (1927) (acq.); I.R.C. § 463.
3. 69 Wis. 2d 723, 233 N.W.2d 354 (1975).

deduction for accrued vacation pay.[4]

The labor contract which obligated the company to make the vacation payments provided that the vacation earning period for employees was from April 1st of one year through March 31st of the next. The contract also provided that if an employee quit or was discharged for cause prior to April 1st, his entire vacation pay would be forfeited. For each of the years 1964 through 1967, Ladish deducted from its gross income an amount reflecting vacation pay which accrued during the first three months of the calendar year as well as that which accrued during the last nine months. The former amount was the amount which vested in the employees on April 1st. The latter amount, however, had neither vested nor been paid during that year and was subject to the forfeiture provision in the labor contract.[5] The Wisconsin Department of Revenue disallowed the non-vested portions of the deductions.[6]

At issue was whether the vacation pay which had theoretically accrued during the last nine months of each year had in fact accrued and was therefore deductible at the end of the calendar year.[7] The court noted that accruability rested not with the certainty of payment but with the certainty of the obligation arising. To determine whether an obligation of payment had arisen the court adopted the so-called "all events" test.[8] Under this test, for an allowable deduction to occur, all events which establish the taxpayer's liability for a specific item must have occurred before the end of the tax year.

In the instant case, the court stressed that Ladish's liability for vacation pay was contingent upon the individual employees

4. Generally, WIS. STAT. § 71.02(1)(c)(1973) permits accrual basis taxpayers to deduct accrued expenses in computing their taxable income.

5. Ladish's accounting method deducted from income vacation pay accruing the last nine months of the taxable year. Any difference between the deduction and the actual payment in the succeeding year was returned to income in that year. Although this method was in accordance with generally accepted accounting principles, the court held that fact was not controlling for Wisconsin income tax purposes and that the proper question was whether or not the company's accounting method clearly reflected its income. *See* WIS. STAT. § 71.11(8)(a) (1973).

6. Amounts disallowed in one year were deductible in the next. Thus, during the period in question, some years resulted in an increase in taxable income and others in a decrease in taxable income.

7. WIS. STAT. § 71.04(7) (1973) provides in material part: ". . . reserves for contingent losses or liabilities shall not be deducted."

8. The "all events" test is said to have arisen in United States v. Andersen, 269 U.S. 422 (1926).

not quitting or being discharged for cause before March 31st. The court thus held irrelevant the fact that the amount of vacation pay annually forfeited was less than one percent of the accrued vacation pay since all the events which fixed the company's liability had clearly not occurred prior to the year end.[9]

Although Ladish Company lost the accruability issue, it did successfully argue that by changing the time when its vacation pay became deductible the court necessarily changed Ladish's method of accounting. Ladish was thus entitled to a vacation pay deduction. Under Wisconsin Statutes section 71.11(8)(b)[10] a taxpayer can offset a 1953 accrual for specific line items against the same item in any year in which its method of accounting is changed.[11] Ladish thus argued that it should be allowed an offset on its 1964 tax return for the accrual of 1953 vacation pay.

In interpreting this complex statute, the Wisconsin court relied heavily on the interpretation of a parallel Internal Revenue Code section.[12] To trigger application of section 71.11(8)(b)

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9. Actually, the amount forfeited was only given for the taxable year ending December 31, 1967. Of the $855,314.38 of vacation pay which was accrued on that date only $3,645.98 was returned the next year.

10. WIS. STAT. § 71.11(8)(b) (1973) provides:

> (b) In computing a corporation's taxable income for any taxable year, commencing after December 31, 1953, if such computation is under a method of accounting different from the method under which the taxpayer's taxable income for the preceding taxable year was computed, then there shall be taken into account those adjustments which are determined to be necessary solely by reason of the change in order to prevent amounts from being duplicated or omitted, except there shall not be taken into account any adjustment in respect of any taxable year to which this section does not apply and except that this rule shall not modify or change the rule as to federal income and excess on its taxes set forth in s. 71.02(1)(c).

11. The reason for permitting adjustment based on the year 1953 is that the present statutory scheme came into being in 1954 and the legislature decided to start fresh for years following 1953. The applicable language within section 71.11(8)(b) is ". . . except there shall not be taken into account any adjustment in respect to any taxable year to which this section does not apply . . ."; that is, 1953. The statute allows, on this basis, a taxpayer to deduct in the year in which a change in accounting method is effected an amount equal to its 1953 accrual for the particular line item changed.

12. Treas. Reg. 1.481-3 (1959) has interpreted the analogous federal provision, I.R.C. § 481(a):

> If the adjustments required by section 481(a) and section 1.481-1 are attributable to a change in method of accounting which was not initiated by the taxpayer, no portion of any adjustments which is attributable to pre-1954 Code years shall be taken into account in computing taxable income. For example, if the total adjustments inthe case of a change in method of accounting which is not initiated by the taxpayer amounts to $10,000, of which $4,000 is attributable to

or its federal counterpart, a change in the taxpayer's "method of accounting" must be made. The issue was, therefore, whether the change in Ladish's treatment of vacation pay amounted to a change in its accounting method. Federal cases have held that a change in accounting method includes a change in the treatment of vacation pay accrual.[13] Furthermore, the term "method of accounting" has been defined by the federal regulations to include not only a complete overhaul of the taxpayer's accounting method but also a change in the treatment of a material item: "A change in method of accounting to which [I.R.C.] section 481 applies includes a change in the over-all method of accounting for gross income or deductions, or a change in the treatment of a material item."[14] The Wisconsin court adopted the federal approach and held that a change in the manner of accounting for Ladish's vacation pay was obviously a change in the treatment of a "material item." An offset was thus allowed on Ladish's 1964 tax return for the accrual of 1953 vacation pay.

The importance of the *Ladish* decision lies in its strict definition of "accrued" liability. In Wisconsin now, no matter how certain the payment of an obligation may be, it will not be deductible as an accrued liability unless all events which "fix the amount of the taxpayer's liability . . . have come about or occurred before the end of the tax year in which the deduction was made."

The "all events" test raises a number of questions. Will otherwise deductible services rendered or supplies delivered before the end of the tax year be held nondeductible if their price has not been set until the next calendar year?[15] Is price

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> pre-1954 Code years, only $6,000 of the $10,000 total adjustment is required to be taken into account under section 481 in computing taxable income. The portion of the adjustment which is attributable to pre-1954 Code years is the net amount of the adjustments which would have been required if the taxpayer had changed his method of accounting in his first taxable year which began after December 31, 1953 and ended after August 16, 1954. See section 481(b)(4)(A), Reg. section 1.481-3.

The net effect of the Wisconsin statute is to allow the taxpayer an offsetting adjustment in the year of a change in accounting method equal to the adjustment that would have resulted if the change had occurred in 1954. That amount would be the 1953 accrual.

13. Oberman Mfg. Co., 47 T.C. 471 (1967), *acq.*, 1967-2 C. B. 3; American Can Co. v. Commissioner, 317 F.2d 604 (2nd Cir. 1963).

14. Treas. Reg. § 1.481-1(a)(1) (1959).

15. It would appear that services rendered or supplies delivered prior to year end,

determination thus an event which could preclude satisfaction of the "all events" test? Would a company's contribution to its profit sharing pension fund after the close of its tax year be nondeductible because it retained the right to revoke the plan at any time, although the amount of the liability had otherwise been determined?[16] Is the nonhappening of an event, such as not revoking a pension or profit-sharing plan, an event which could prevent satisfaction of the "all events" test? These questions were not clearly answered in *Ladish* and should be considered when determining whether a liability has accrued in Wisconsin.

II. INHERITANCE TAXATION OF JOINTLY-HELD PROPERTY

In Wisconsin, prior to 1972, an inheritance tax was automatically assessed on the fractional interest of the survivors in an amount determined by dividing the market value of the property by the number of joint tenants at the time of death.[17] When the Wisconsin inheritance tax was amended in 1972,[18] Wisconsin adopted the federal approach to taxing jointly owned property on death.[19]

The amended survivorship statute, Wisconsin Statutes section 72.12(6)(a),[20] provides that when an owner of property sub-

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but not fixed as to price, probably would be deductible in the year of delivery as the certainty of the obligation was fixed. However, it can be argued that an event, the setting of the price, precluded fixing the "amount" of the liability prior to year end and therefore the amount is not deductible.

16. *See*, Aunt Nellie's Foods, Inc. v. Department of Revenue, 8 W.A.T.C. 264 (1971) (affirmed by Dane County Circuit Ct., August 19, 1971).

17. WIS. STAT. § 72.01(6) (1969).

18. 1971 Wis. Laws, ch. 310.

19. *See* I.R.C. § 2040. Under this approach a tax is levided only on the deceased's contributions to the joint tenancy.

20. WIS. STAT. § 72.12(6) (1973) reads:

(6) SURVIVORSHIP INTERESTS. (a)*Rule.* When property is held in the names of 2 or more persons with the right of survivorship, upon the death of one of the persons. Transfer of the full clear market value of the entire property is subject to this subchapter.

(b) *Exceptions.* If the property or the consideration with which it was acquired, or any part of either, is shown to have originally belonged to the survivor and never to have been received or acquired by him from the decedent for less than adequate and full consideration in money or money's worth, the transfer of the property or the part originally furnished by the survivor is not taxed. If the property was acquired by gift, bequest, devise or inheritance by the decedent and any other person, the taxable portion is determined by dividing the clear market value of the property by the number of owners, unless the instrument creating this ownership creates interests in a different proportion.

ject to the right of survivorship dies, the entire value of the jointly held property is subject to an inheritance tax, with only two exceptions.[21] The first exception, which is the basis of the present controversy, exempts from inheritance taxation that portion of the property which originally belonged to the survivor and had not been "acquired by him from the decedent for less than adequate and full consideration in money or money's worth . . . ."[22]

In re Estate of Kersten[23] involved a petition by a widow for redetermination of the inheritance tax payable on the estate of her deceased husband. She claimed she had made significant contributions in the form of personal services which constituted consideration in money's worth and which had led to the acquisition of the jointly held property in the estate. The widow and her husband had spent all of their married lives operating their family farm.[24] Although there had never been any written

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21. After *In re* Estate of Kersten, WIS. STAT. § 72.12(6)(a) was again amended. The new statute reverted to the former practice of assessing an inheritance tax, when jointly-owned property is involved, on the fractional interest of the survivors determined by dividing the property's market value by the number of joint tenants. 1975 Wis. Laws ch. 222. The new section states:

> (6) SURVIVORSHIP INTERESTS. (a) *General provision.* When property is held in the names of 2 or more persons with the right of survivorship but not as tenants in common. Upon the death of one joint tenant, the right of the surviving joint tenant or tenants to the immediate ownership or possession and enjoyment of such property shall be deemed a transfer taxable under this subchapter at the property's clear market value.
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> (b) *Joint tenancy exemption.* When property is held in the names of 2 or more persons with the right of survivorship, the following shall be subtracted as provided in par. (c):
>
> (1) The fractional interest of the survivor or survivors in property in an amount determined by dividing the property's clear market value by the number of joint tenants, including the decedent, except as provided in subd. 2.
>
> . . .
>
> (c) *Application of exemption.* The amount determined in par. (b)2 shall be subtracted from the amount determined under par. (a) prior to application of the tax rates under s. 72.18. The amount determined in par. (b)1 shall be added to the exemption allowzd under s. 72.17(1) to (3) and shall be applied to the lowest tax bracket or brackets under s. 72.18. The remaining tax rates shall then be applied to the balance of property, the transfer of which is taxable under this subchapter, beginning at the tax rate applicable to the bracket in which the exemptions end.

22. The other exception, provided in WIS. STAT. § 72.12(6)(b), which is not at issue here, exempts from inheritance taxation property acquired by the decedent and the survivor jointly by gift, bequest, devise or inheritance.

23. 71 Wis. 2d 757, 239 N.W.2d 86 (1976).

24. The petitioner was credited with maintaining the household, keeping the books, training the calves, assisting with the milking and baling and generally assisting

partnership agreement, the couple operated the farm as a team and could not have done so without the help of the other. The court faced two issues on appeal:

> 1. Did the wife's personal services in assisting with the farm operation constitute consideration in "money or money's worth" in return for her interest in the jointly held property?
> 2. If so, by what amount should the value of the jointly owned property be reduced for inheritance tax purposes?

In addressing these issues the court defined "consideration in money or money's worth" as "such consideration as is reduceable to a money value or is capable of being valued in terms of money."[25] The court noted the legislature's obvious attempt to pattern section 72.12(6) after section 2040 of the Internal Revenue Code which reflected a clear intent "to tax the transfer of jointly-held property in the same manner as the federal method."[26] Relying on a prior federal tax court case with similar facts, the court thus held that the widow's continuing contribution in the way of service, industry and skills to the operation of the farm constituted a contribution "in money's worth" in the production of joint income which was used to acquire the jointly held assets.[27]

The court neatly avoided the question of valuating the widow's services. It decided that once it had been found that the services constituted adequate and full consideration in money or money's worth for the survivor's interest in the property, it was not necessary to valuate those services. The value of the jointly held property subject to inheritance tax should be reduced to the extent of the survivor's fractional interest. The widow was thus held to have contributed one-half of the consideration for the jointly owned farm property.

The obvious question raised by *Kersten* in whether domestic services performed by wives constitute contributions on their part to jointly owned property. Application of the Wisconsin definition of "consideration in money or money's worth" could provide a persuasive argument that domestic services constitute a contribution on the wife's part. Many domestic services performed by wives could arguably be "reduceable to

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in the operation of the farm. She twice ran the farm alone while her husband was sick.

25. 71 Wis. 2d at 763, 239 N.W.2d at 90.

26. 1971 Wis. Laws, ch. 310 at 1246.

27. Estate of Everette Otte, 31 T.C.M. (CCH) 301 (1972).

a money value" or are "capable of being valued in terms of money," and, therefore, should logically constitute a contribution on a wife's part to jointly owned property. Whether *Kersten* justifies this conclusion is questionable.

Kersten indicates that the construction given by the federal courts to parallel federal provisions should be given considerable weight. It appears fairly clear under federal interpretation of section 2040, that the ordinary domestic services provided by spouses do not constitute a contribution to jointly held property.[28] Under the federal scheme, however, if a wife aids her husband in his business under an agreement to share profits, she generally will be deemed to have contributed part of the consideration for the purchase price of property acquired with the profits of the business.[29] *Kersten* has gone one step further in not requiring any type of business agreement. In *Kersten*, there was no partnership profit-sharing agreement, nor did Mrs. Kersten ever report personal income for income tax or social security purposes. The nature of her services, however, as those in the federal cases, was recognized as primarily business related.

As noted, *Kersten* specifically held that the wife's services had contributed to the production of "joint income" which had been used to acquire the jointly held assets. Generally, however, a wife's domestic services do not produce income with which the couple purchases property. *Kersten* would, therefore, have no precedential value for a case in which a spouse's contribution was solely in the nature of domestic services. Due to Wisconsin's expressed policy of following federal court constructions of parallel federal estate tax statutes, and since a spouse's domestic services generally do not produce income, it is doubtful whether Wisconsin will recognize a contribution toward jointly held property for purely domestic or household services provided by the surviving joint tenant.[30]

III. GIFTS BY IMPLICATION

The Wisconsin Supreme Court reviewed and applied the

28. *See* Bushman v. United States, 8 F. Supp. 694 (Ct. Cl. 1934), *cert. denied*, 295 U.S. 756 (1935); Estate of H.C. Loveland, 13 T.C. 5 (1949).

29. United States v. Neel, 235 F.2d 395 (10th Cir. 1956); Berkowitz v. Comm., 810 F.2d 319 (3d Cir. 1939). *Cf.* Singer v. Shaughnessy, 198 F.2d 178 (2d Cir. 1952).

30. Of course, given Wisconsin's reversion to the automatic inclusion approach, this question may be moot in many cases.

doctrine of "gift by implication" in *In re Trust of Pauly.*[31] The doctrine of "gift by implication"[32] is "the ascertainment of the intention of the testator from all the words used in the will in the light of surrounding circumstances to fill in a void or an omission in the expressed terms of the will."[33] The doctrine is one of three methods of judicial action used when a will's directions are not plain, explicit and capable of being readily followed.

The sole goal in the transfer of property as directed by a will is to carry out the expressed interest of the testator. Normally this requires the mere following of the will's directions. However, in some wills the directions are incomplete, inconcise, or contrary to the obvious intent of the testator. Problems are generally in the nature of ambiguities,[34] mistakes,[35] or omissions.

The term "construction of the will" has been used in the resolution of each of the above stated problems.[36] In *Pauly,* the testatrix's will directed that her daughter receive trust income

31. 71 Wis. 2d 306, 237 N.W.2d 719 (1976).

32. The doctrine of gift by implication originated in Wisconsin in *In re* Donges's Estate, 103 Wis. 497, 501, 79 N.W. 786, 787 (1899). According to *Donges* the doctrine is the result of the application of three basic principles used in determining the intention of the testator:

> First, that in case of doubt such construction will be adopted as to support and give effect to the will, rather than to defeat it; second, that a testator is presumed to have intended a complete distribution of his estate, and a construction tending to that end will be preferred to one which results in intestacy as to any part.

33. Estate of MacLean, 47 Wis. 2d 396, 406, 177 N.W.2d 874, 879 (1970).

34. An ambiguity has been defined as "language in a will which is unclear and requires judicial construction to determine its meaning." Estate of Connolly, 65 Wis. 2d 440, 459, 222 N.W.2d 885, 895 (1974) (Hansen J., dissenting). Justice Hansen's analysis in his dissent in *Connolly* appears to have been adopted by the court in *Pauly.* The *Pauly* decision not only delineated the differences between ambiguities and omissions, but carefully pointed out that the analysis done by courts in deciding whether or not to apply the doctrine of gift by implication was not "construction." Both of these were key points in Justice Hansen's analysis.

35. Justice Hansen defined "mistake" as "a mistake in a will, as in matters of identification of property or beneficiaries." Estate of Connolly, 65 Wis. 2d 440, 459, 222 N.W.2d 885, 895 (1974).

36. *See, e.g.,* Will of Wehr, 36 Wis. 2d 154, 152 N.W.2d 868 (1967) (The court "construed the will to determine the meaning of the ambiguously used word 'descendant'."); Estate of Gibbs, 14 Wis. 2d 490, 111 N.W.2d 413 (1961) (The court corrected a mistake as to named legatee and referred to such reformation as construction); Estate of Maclean, 47 Wis. 2d 396, 177 N.W.2d 874 (1970) (The court applied the doctrine of gift by implication and referred to it as a "construction" adopted to give effect to the will).

for life. If the daughter died before her son (the testatrix's grandson) reached the age of thirty, the trust income was to be paid equally to her son and daughter (the testatrix's grandchildren) until the son reached thirty years of age. The trust would then cease and the principal would be divided equally between the brother and sister. However, the income beneficiary lived past her son's thirtieth birthday and then outlived her daughter, who was survived only by her husband. The contingency that the income beneficiary would die after her son attained the age of thirty was not anticipated in the will. When the income beneficiary renounced her income rights and assigned all her interest in the trust res to her son, the trustee petitioned court for "construction."

The court rejected the contention that the omission created a reversionary interest in the testatrix and held that "the proper course is to note that the provision is silent under the circumstances, and that the court may review the will to see if the gap is filled by implication."[37] The court stressed that such scrutiny was not "construction," and that the omission of a circumstance was not an ambiguity of language.[38] The critical issue was whether the doctrine of gift by implication was applicable.

The general scheme of the testatrix's will in *Pauly* provided a means of ultimate disposition of the trust property if the income beneficiary died before her son attained the age of thirty. Applying the doctrine of gift by implication, the court held that it was the testatrix's intent that the same order of distribution be followed if the income beneficiary died after her son reached age thirty. The income beneficiary was thus precluded from assigning the entire trust res to her son.

The doctrine of gift by implication may depend entirely upon a judge's view as to whom the corpus should be distributed. It does, however, provide a method to rectify a drafting oversight or to salvage imprecise wills which nevertheless evince an overall testamentary intent.

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37. 71 Wis. 2d at 311, 237 N.W.2d at 722.

38. The entire *Pauly* opinion was consistent with Justice Hansen's analysis of the difference between ambiguities, mistakes, and omissions in Estate of Connolly, 65 Wis. 2d 440, 222 N.W.2d 885 (1974) (dissenting opinion).

IV. Fiduciary Duty of Personal Representative

Personal representatives are frequently given, by the decedent, a power of sale over the estate property without court authority. This power is a trust power not to be exercised with arbitrary discretion or for the benefit of the personal representative.[39] It has often been recognized that the personal representative must act not only with good faith in the exercise of this power, but also with loyalty to the beneficiaries of this power.[40] *In re Estate of Meister*[41] presented the question of when a personal representative may be surcharged for negligent exercise of his duty. The personal representative was charged with negligent management and sale of the decedent's Wisconsin real estate, all of which was income producing.

The court made clear that mere negligence on the part of the personal representative will not expose him to personal liability unless the beneficiaries prove a harm to the estate, *i.e.*, either a loss in value of the estate property or loss of anticipated profit by retaining the property. Most importantly, the court voted that there could be no surchargeable loss if at the time estate property was sold the sale was necessary for liquidity purposes. This was precisely the situation in the case where the evidence indicated that the decedent's real estate comprised eighty percent of the estate's assets while the estate's cash requirements equaled two-thirds of this amount.

John L. Schliesmann

TORTS

I. Products Liability

The supreme court issued several significant opinions in the area of products liability during its 1975 term. In *Greiten v. La Dow*[1] the court once again attempted to isolate and clarify the requirements for a cause of action sounding in negligence as

39. Estate of Scheibe, 30 Wis. 2d 116, 140 N.W.2d 196 (1966).
40. Estate of Van Epps, 40 Wis. 2d 139, 161 N.W.2d 278 (1968); McKeigue v. Chicago & N.W. Ry., 130 Wis. 543, 110 N.W. 384 (1907).
41. 71 Wis. 2d 581, 239 N.W.2d 52 (1976).

1. 70 Wis. 2d 589, 235 N.W.2d 677 (1975).