SOME RECENT DEVELOPMENTS IN WISCONSIN INCOME TAXATION

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THERE is probably no field of law where development and change is as rapid as in the field of income taxation. Legislative enactments completely revamping existing income tax acts come with depressing frequency as expressions of the constant change in economic conditions and of the varying political conceptions of the party which happens to be in power. Courts interpreting these new and partially experimental statutes necessarily have little precedent to guide them and in sailing their uncharted courses frequently pilot their ships into the most unexpected shoals. The three changes to which this article is restricted—one legislative and two judicial—all occurred within the last six months and it is believed are typical of the rapid change of policy and interpretation to which our income tax laws are subject.

A so-called "unemployment relief income tax" was enacted by the legislature and became effective as Chapter 29, Laws of the Special Session of 1931, on February 8, 1932. It provided for a special and additional tax on 1931 incomes of individuals at the same rates as provided by the current state income tax act, but to increase the tax base two innovations were introduced. First, dividends from Wisconsin corporations were not exempted for the first time in our tax history and, second, both gains and losses on the sales of securities, real estate or other property were to be excluded in measuring net income.

The latter provision raises an interesting constitutional question. Let us assume that A in 1931 purchased with his entire savings $15,000 worth of stock, borrowing $5,000 from his bank to make up the needed fund. Let us further assume that A had a salary during the year of $5,000 and that before the year was over his stock became worthless and was sold. His net loss as ordinarily and as heretofore computed would be $10,000, but under the new law he would be taxed on his $5,000 salary as income, notwithstanding that the net result of his year's operations was to wipe out his entire estate and leave him insolvent to the extent of $5,000. Does Article VIII, Section 1 of the Wisconsin Constitution, which authorizes progressive taxes on incomes, permit the legislature to define income so as to include only certain profits and to exclude certain losses and thus arrive at a taxable income as variant from the real facts as in the above example?

The United States Supreme Court has several times stated "that

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which is not in fact the taxpayer's income cannot be made such by calling it income.” (See Hoeper v. Tax Commission, 284 U.S. 206 [215]). In view of the large sums involved, the question will almost certainly be presented to the courts.

Other provisions of the new act require the distribution of the proceeds to the various counties, cities, towns and villages of the state to be used for outdoor relief and any portions not used are to be applied to a reduction of the general property taxes of the municipal corporation concerned for 1933. There is certainly considerable doubt as to whether this use of state raised taxes to defray county or city expenses can be justified under Article VIII, Section 5 of the Constitution which provides that “The legislature shall provide for an annual tax sufficient to defray the estimated expenses of the state for each year.”

An interesting milestone in the development both of income tax law and the emancipation of women is the United States Supreme Court decision of Hoeper v. Tax Commission, 248 U.S. 206, (Nov. 30, 1931) reversing the decision of our Supreme Court found in 202 Wis. 493, 233 N.W. 100. Section 71.05 (2) (d) of our statutes had required the computing together of the husband's, wife's and children's income in any family for the purpose of rates and exemptions, thus throwing more income into higher brackets than if they were computed separately. The United States Supreme Court took the view that since under our Wisconsin Married Women Acts the husband has no right to or control over the wife's income, to use her income to affect the rates for his tax is “to measure his tax, not by his own income, but by that of another” and that to so do “is contrary to due process as guaranteed by the Fourteenth Amendment.” Justice Brandeis and Stone concurred in a very characteristic dissenting opinion written by Justice Holmes who felt that the legislature could properly consider that while the husband no longer had command over the wife's income, her income in fact would “make his life easier and help to pay his bills.”

A decision of more general scope, and which has caused considerable consternation in the ranks of tax practitioners is the decision of the Wisconsin Supreme Court in Whitbeck v. Tax Commission, (Dec. 1931), 239 N.W. 655, rehearing opinion (Feb. 1932), 240 N.W. 804. The United States Supreme Court in Long v. Rockwood, 277 U.S. 142, 48 S. Ct. 463, had held that patent royalties were not subject to state income tax. Accordingly, the plaintiff, who had reported certain copyright royalties on his income tax return and had paid a tax on them, filed a claim for refund, following the statutory procedure applicable to refunds, and the same procedure which had been followed
in a number of other refund cases where taxpayers had prevailed in the Supreme Court without question as to the technical prerequisites of the refund claim being raised.

The statutory procedure requires the taxpayer to file a refund claim within the statutory period with the Assessor of Incomes (or with the Tax Commission in the case of corporations) and if the claim be denied, prosecute an appeal to the Circuit Court after hearing before the County Board of Review and the Tax Commission under Section 71.16 of the statutes. This procedure entailed administrative action on the claim prior to court review and seemed thus to follow the general scheme of the statutes.

In the Whitbeck case the court, however, for the first time directed its attention to a provision of 71.17 (5) which by an obscure reference to Section 71.14 seemed to make an appearance by the taxpayer before the income tax board of review within twenty days after the income tax in question is assessed a prerequisite to a refund of the erroneously reported and assessed tax. On rehearing it was urged on the court that as income taxes based on March 15th returns are assessed by June 1st, and the Board of Reviews does not meet until the last Monday of July, the procedure was not applicable and could not have been intended by the legislature to govern refund cases. On rehearing, however, the court not only stood its ground, but went a step further holding that as a result of its conclusion a taxpayer who had erroneously reported income on his return "has no right to a court review to correct that error" and that in filing his return there is imposed on

"the taxpayer the duty of correctly assessing himself at his peril. In case he does overtax himself his only remedy is that provided by subsections (5) and (6) of Section 71.10 and by filing a claim for refund. Section 71.17(5) If the reviewing authority refuses to certify any overpayment, the taxpayer is without other remedy."

Thus the court has apparently completely abrogated legally enforceable refund claims for erroneously reported income and in interpreting the letter of the refund statute has pretty well done the statute itself to death. If a citizen erroneously reports too little income, the state can correct the error and enforce the collection, but if the citizen erroneously reports too much, he is without court relief. Such an anomaly is shocking to one's sense of justice.

That the statute contemplated that in making a return there was imposed upon the taxpayer the duty of "assessing himself at his peril" seems a conclusion hardly warranted by an examination of the statutes themselves particularly considering the purposes of a refund. A provision for refund is granted taxpayers to permit them, within a certain statutory period, to recover taxes erroneously reported. Everyone
knows that questions as to whether certain expenditures are capital or income, whether, if income, they are taxable, or whether the particular income is applicable to one calendar year or another, are questions that no taxpayer can in fairness be expected to know at the time of preparing his return. In fact, subsequent events, not known at the time of the return, often establish that particular items returned by a taxpayer were not in fact income although believed by all concerned to be income at the time reported. For these reasons the legislature incorporated a refund provision in the statutes with a court review.

Returns are made on forms provided by the state. The taxpayer is required to fill out the forms fully or be subject to penalties. Now to hold that in giving the state in good faith the information demanded of him he is assessing himself and waiving his legal remedies in case of error, seems to be a result entirely inconsistent with the very object of a refund statute. The statement of the court that "an objection to an assessment is one thing and an objection to a tax levied pursuant thereto is another" would seem to indicate that the court in interpreting these provisions confused the principles of real estate and income taxation as it is difficult to see what the comment of the court can mean as applied to income taxes.

A more disturbing and fundamental consequence of the decision is to give to the Tax Commission an unreviewable discretion over refunds. If the words of the decision are to be taken at their face value, they mean that the Tax Commission can grant a refund to Smith and deny it to Jones on the same set of facts, or grant it to its friends and deny it to its enemies, or grant it to Republicans and deny it to Democrats or vice versa, without any court review being available for the rejected claimant. The vesting of such arbitrary and unbridled power in an administrative commission is certainly foreign to all our usual conceptions of administrative action and seems to authorize policy of administrative tyranny contrary to our traditional government of law and not of men.

The decision is the more surprising coming from a court which has hitherto taken an energetic position against the ever growing encroachment of commission and bureaucratic government. It is earnestly to be hoped that either the legislature will, by prompt enactment, restore to taxpayers a workable refund statute with a court review or that the court itself will modify its pronouncement in the next case coming before it.