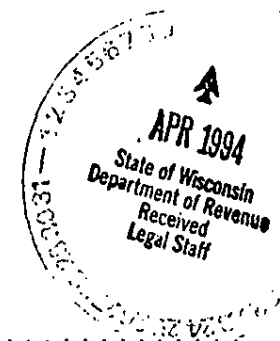


MAULE MARY L 92I327 040894 TAC



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STATE OF WISCONSIN
TAX APPEALS COMMISSION

MARY L. MAULE	*	
Rt. 1, Box 260	*	DOCKET NO. 92-I-327
Cecil, WI 54111	*	
	*	RULING AND ORDER
Petitioners,	*	
	*	
vs.	*	
	*	
WISCONSIN DEPARTMENT OF REVENUE	*	
P.O. Box 8933	*	
Madison, WI 53708	*	
	*	
Respondent.	*	

JOSEPH P. METTNER, COMMISSIONER:

This matter is before the Commission for ruling based upon the petitioner's motion for partial summary judgment, which was filed with the Commission on February 1, 1993, and which was subsequently clarified as to issues and scope during the October 6, 1993 hearing held on the motion. Both parties have also submitted affidavits, exhibits, and briefs in support of their respective positions.

The petitioner was represented by Attorney Karen A. Case, from the law firm of Case, Drinka & Diel, S.C., of Milwaukee. The respondent was represented by Attorney Lili Best Crane.

Based upon the affidavits, exhibits, and briefs submitted by the parties, this commission makes the following

FINDINGS

1. During the years 1986 and 1987 ("the period under review"), the petitioner was married to Gerald L. Maule. The

petitioner and her husband filed joint Wisconsin income tax returns during 1986 and 1987, including information from the couple's federal Form 1040, Schedule C relating to activity from Mr. Maule's charter boat business.

2. Prior to 1986, Gerald L. Maule had spent two seasons (i.e. Memorial Day through Labor Day) working on a charter fishing boat owned by Earl Kahler and chartered out of Algoma, Wisconsin. Mr. Maule's primary source of income until his death in 1988 was a salary earned as a customer service representative for the Carnation Can Company, where he earned approximately \$31,800 annually, according to exhibits accompanying the petitioner's affidavit.

3. During 1985, Gerald L. Maule spoke with some of the owners of the estimated 30-35 charter boats docked at Pier 42 in Algoma while exploring the prospect of purchasing his own charter boat. Mr. Maule also spoke with loan representatives of the Citizens State Bank in Shawano, Wisconsin concerning potential financing for a planned charter boat purchase.

4. The petitioner recollects that her husband had calculated a "break even point," or an estimated minimum level of revenue required to realize positive cash flow from chartering, of 40-50 half-day charters during a 180-210 half-day season from Memorial Day to Labor Day. The petitioner recalled in particular that Mr. Maule's projections included consideration that a licensed captain would need to be hired on each charter trip because Mr. Maule was not, at the time, a licensed charter captain. No

reproduction of these calculations has ever been provided by the petitioner to the Internal Revenue Service or the respondent.

5. Sometime in 1985, the Maules obtained the necessary financing from the Citizens's State Bank of Shawano and purchased a 32-foot, wooden hulled, twin engine, 1967 Chriscraft boat. The name of the boat was "Silly Girl IV." According to the petitioner, Mr. Maule intended to build a charter fishing business, take early retirement, and supplement his retirement income with charter fishing profits.

6. In 1986, Gerald Maule purchased a second charter boat. The second boat was a 36-foot Chriscraft Roamer with a steel hull. Mr. Maule later sold his first boat, the 32-foot Chriscraft, in April of 1987 to avoid incurring the added expense of chartering or maintaining two boats throughout the 1987 charter season.

7. During the 1986 charter season, Gerald Maule worked closely with Earl Kahler in managing the Maule charter boat business. Mr. Kahler was one of three licensed charter captains affiliated with the "Silly Girl Charter Service." The other licensed captains affiliated with the charter service were Ron Szymanski and Karl Hough. Kahler, Szymanski, and Hough chartered their respective craft out of Pier 42 in Algoma, as did Gerald Maule, through the Silly Girl Charter Service. Maule shared expenses for the printing of promotional pamphlets and the placement of advertisements in shopper's guides with the other members of the Silly Girl Charter Service. One such pamphlet notes a \$50.00 hourly rate for charter service for parties of up to 6

people.

8. The petitioner maintains that Gerald Maule set up a separate bank account for his chartering business at the Citizens State Bank. The petitioner also maintains that Gerald Maule kept a separate record of charter income and expenses and a charter customer log. This log has never been located by the petitioner or shared with either federal or state revenue authorities, because it was lost after Mr. Maule's death in April of 1988.

9. To some extent, Mr. Maule intermingled his charter income and expense accounting with the business income and expense accounting of Earl Kahler during 1986. Earl Kahler helped to manage Gerald Maule's charter activity in addition to managing his own boat, the Calm Seas, through the Silly Girl Charter Service. A rough expense sharing method was used by Mr. Maule and Mr. Kahler during 1986. The method entailed Mr. Maule advancing cash to Earl Kahler for use in the management of Maule's charter boat. Earl Kahler then incurred day-to-day operating expenses, some of which were 100% allocable to the Maules' craft. General supply expenditures were shared on a pro rata basis, with Kahler allocating 1/3 of the expense to his charter operation and 2/3 to Mr. Maule's craft, a split determined according to the relative levels of use of each charter craft. Expenses which benefitted the separate craft equally, such as those incurred for participation in sporting shows, were allocated 50-50 between Mr. Maule and Mr. Kahler. In 1987, Mr. Maule assumed sole responsibility for all income and expense items associated with his charter craft

activity.

10. Gerald Maule undertook all maintenance expenses and general upkeep and repair of his charter craft personally, using his evenings and weekends to do so.

11. The Maules took no more than four personal trips annually aboard Mr. Maule's charter craft, with Mr. Maule spending substantial amounts of time on these trips tuning the boat's engine. The Maules' two teenage children were allowed one personal trip each per year to entertain friends on the boat. These trips were scheduled during weekdays, with weekend priority given to paying, third-party charters. Any additional access to the boat by the Maules as a family was limited to repainting the hull, putting in the boat for docking at the beginning of each season, and removing the boat from Algoma at the end of the season.

12. During the fall of 1987, Gerald Maule completed the requirements to obtain a charter captain's license. Mr. Maule died in April of 1988, while working on his boat.

13. Schedule C information submitted with the petitioner's federal Form 1040s for 1985, 1986 and 1987 noted the following with respect to Mr. Maule's charter fishing business:

<u>Year</u>	<u>Gross Receipts</u>	<u>Net Loss</u>	<u>Depreciation</u>
1985	\$ 8,250	\$ (7,311)	\$ 1,932
1986	21,897	(28,244)	11,588
1987	6,635	(20,244)	10,410

The petitioner contends that the downturn in gross receipts experienced during the 1987 fishing season was due to a PCB (polychlorinated biphenyl) scare on Lake Michigan, apparently

causing fear of fish contamination.

14. The Maules' 1986 and 1987 federal income tax returns were audited by the Internal Revenue Service. This audit process culminated in a settlement agreement which was signed by the petitioner, dated March 23, 1991. The terms of the settlement allowed the Maules 50% of the Schedule C charter business expense deductions taken on the returns as originally filed. The downward adjustment in expenses allowable to the petitioner resulted in deficiencies of income tax due to I.R.S. in the amounts of \$3,450 for 1986 and \$2,437 for 1987.

15. The petitioner's representative notified the respondent of the federal settlement in a letter dated May 9, 1991. The letter raised a defense under the Wisconsin Statutes to the applicability of the agreed upon federal adjustment to the petitioner's Wisconsin taxable income.

16. The respondent issued an assessment against the petitioner in a notice dated August 19, 1991, based upon the I.R.S. adjustment of the petitioner's 1986 and 1987 federal taxable income agreed upon by the petitioner. The assessment was based upon federal audit workpapers, including federal appeal correspondence and memoranda obtained from the I.R.S.

17. Through her representative, the petitioner petitioned the respondent for a redetermination of the assessment in a letter dated August 26, 1991.

18. The respondent issued its notice of action in a letter dated June 22, 1992, in which it denied the petitioner's

petition for redetermination.

19. The petitioner filed a timely petition for review with this commission on July 7, 1992.

20. There is no genuine issue of material fact before the Commission with respect to the issue of whether the business of the petitioner's late spouse was an "activity not engaged in for profit."

21. Pursuant to § 802.08(2), Stats., the petitioner is entitled to summary judgment as a matter of law because the charter fishing business of the petitioner's late spouse, Gerald Maule, did not constitute an "activity not engaged in for profit" under § 183 of the Internal Revenue Code during the years under review.

OPINION

The petitioner in this case has moved for partial summary judgment on the issue of whether her late husband's charter fishing business was an activity not engaged in for profit under I.R.C. § 183. We find that the relevant facts and circumstances in this case, submitted by the parties through affidavits and exhibits, remain uncontroverted in any material way. Only the legal conclusions drawn from these facts by the parties differ. In total, the relevant facts and circumstances submitted by the parties demonstrate that Gerald Maule's charter fishing business was not an "activity not engaged in for profit" under I.R.C. § 183 for the period under review. Therefore, the limitation upon business deductions imposed by § 183 does not apply to the petitioner for those years.

The definition of an activity not engaged in for profit is detailed in Treas. Reg. § 1.183-2. In particular, Treas. Reg. § 1.183-2(b)(1)-(9) offers nine "relevant factors" tending to indicate the presence of an activity not engaged in for profit. Under the Regulation, these factors are not to be considered an exhaustive list of relevant factors. "In determining whether an activity is engaged in for profit, all facts and circumstances with respect to the activity are to be taken into account. No one factor is determinative..." Treas. Reg. § 1.183-2(b).

The notion that no single factor is determinative of an activity's status under § 183 is significant for purposes of summary judgment analysis in this case, because the parties disagree, in relevant part, only upon inferences of ultimate fact concerning the "manner in which the taxpayer carried on the activity," one of the nine elements offered in the Regulation. Treas. Reg. § 1.183-2(b)(1). Elements of this single factor include whether the taxpayer carried on the activity in a businesslike manner and maintained complete and accurate books and records. Id.

The petitioner has contended that her husband kept a separate bank account for charter activity during at least part of the period under review, and also maintained a log of charter customers and expenses. The respondent has countered that the petitioner has the burden of proof in this matter, absent the application of the presumption of § 183(d). On the basis that no charter log pages or bank account records have ever been provided

by the petitioner to any revenue authorities, the respondent concludes that Mr. Maule's charter business was not run in a businesslike manner and is, accordingly, an activity not engaged in for profit.

We do not find that these countering contentions of the parties produce a joined, genuine issue of material fact precluding summary judgment in this case. The petitioner attests that her husband established a separate bank account for his charter service, and kept a customer and expense log. Both parties agree that these records were unable to be located during the I.R.S. audit for verification, and have not been subsequently provided to the respondent.

In short, none of the constituent *facts* relating to the lost documents are disputed. It is the respondent's *contention by inference* of the ultimate fact that the charter service of the petitioner's late spouse was not run in a businesslike manner, which is disputed.

Ample, uncontroverted facts support our finding that the charter fishing business at issue was run in a businesslike manner. Gerald Maulé initially placed much of his charter fishing operation in the hands of individuals who were knowledgable in the business. There are two practical reasons for this decision. First, Mr. Maule was learning the business and needed to start at some point by entrusting his fairly expensive asset to those with more expertise. Second, Mr. Maule was not a licensed charter fishing

captain for fishing seasons during the period under review.¹ This was one of the key reasons for his affiliation with the Silly Girl Charter Fishing Service, whose other members were licensed captains. This affiliation also enabled Gerald Maule to advertise charter services in pamphlets and publications. Mr. Maule and Mr. Kahler also promoted their charter services through participation in sports shows. After sharing responsibility for expense accounting for his charter business with the Kahlers during the

¹ This point is worth further elaboration, because it bears significantly upon the issue of Mr. Maule's businesslike practices, the practical difficulties of entering the charter fishing business, and the respondent's contention by affidavit that Mr. Maule filed no sport trolling reports during the period under review.

Under the United States Coast Guard Regulations, licensure is required for one to become the pilot or captain of an uninspected passenger vessel for hire carrying six or fewer passengers on the Great Lakes. See, 10 C.F.R. 466(d) Successful completion of a written examination and the equivalence of twelve months experience are prerequisites to obtaining a license. Id. One must have a Coast Guard operator's license number in order to apply to the Department of Natural Resources (DNR) for a sport trolling license for use on Lake Michigan, Lake Superior, or Green Bay. § 29.166(1), Stats. Only those licensed with the DNR are required to file monthly sport trolling reports to the DNR. § 29.166(2), Stats.

Gerald Maule clearly needed to retain a duly licensed charter fishing captain in order to let his boat for hire in the charter fishing business on Lake Michigan. Otherwise, his asset, the fishing boat, could not generate a revenue return. At the same time, Mr. Maule had to serve a practical apprenticeship aboard a charter fishing vessel before obtaining a charter fishing captain's license, which he accomplished following the 1987 fishing season. Given the Coast Guard's experience equivalence requirement, it is not surprising that Mr. Maule served three fishing seasons working part-time under others in order to fulfill this prerequisite. It was also a clear financial advantage to Mr. Maule to work toward captaining his own boat to reduce expenses.

Until he became a licensed charter captain, Mr. Maule was not required by law to file monthly trolling reports. Only his retained captains had this responsibility under § 29.166(2), Stats.

Unfortunately for Mr. Maule, his life did not extend to meet his ambitions for his business.

1986 season, Mr. Maule assumed these duties himself. In 1986, Mr. Maule upgraded his craft from a 32-foot, wooden hull vessel to a 36-foot, steel hull craft. In 1987, Mr. Maule obtained his charter captain's license. These uncontroverted facts demonstrate that Gerald Maule's sophistication in managing his charter fishing business continued to grow with his experience in the business. This is not uncommon in the operation of small businesses. We are satisfied that the charter fishing affairs of Mr. Maule were managed in a businesslike manner.

With respect to examining the application of other "relevant factors" noted in Treas. Reg. § 1.183-2(b), we find that those listed factors which are not made irrelevant by the specific facts of this case also contribute to our overall conclusion that Mr. Maule's charter fishing business was not an "activity not engaged in for profit."

The factors detailed in Treas. Reg. § 1.183-2(b)(4) and (5), "expectation that assets used in the activity may appreciate in value" and "the success of the taxpayer in carrying on other similar or dissimilar activities," respectively, are irrelevant to this case and do not figure in our analysis. This is because charter fishing boats, like cars or trucks, only diminish in value over time after being placed in service, and Mr. Maule carried on no "similar or dissimilar activities" under the facts submitted by the parties.

An examination of the factors detailed in Treas. Reg. § 1.183-2(b)(2) and (3), "the expertise of the taxpayer or his

advisors" and "the time and effort expended by the taxpayer in carrying on the activity," respectively, favors the taxpayer for many of the same uncontroverted factual reasons noted in our analysis of the businesslike manner of Mr. Maule's conduct of his charter fishing business. It is undisputed that Messrs. Szymanski, Hough, and Kahler, affiliates of Mr. Maule in the Silly Girl Charter Service, were all licensed charter captains. These individuals were consulted, along with other owners of Algoma's Pier 42 fishing craft and a Shawano banker, prior to the purchase of Mr. Maule's first craft. Mr. Kahler in particular remained an active advisor and manager of Mr. Maule's craft after the purchase. It is also undisputed that Mr. Maule spent significant amounts of time maintaining his craft and assisting on charter cruises. Were this latter fact not true, Mr. Maule could not have obtained his own charter captain's license under U.S. Coast Guard Regulations.²

An examination of the factors detailed in Treas. Reg. § 1.183-2(b)(6) and (7), "the taxpayer's history of income or losses with respect to the activity" and "the amount of occasional profits, if any, which are earned," respectively, favors the petitioner, given that the years under review were clearly start-up years in the progression of Mr. Maule's charter business. Although Mr. Maule realized net losses for each of the years he operated the charter business, including 1986 and 1987, he had only begun operating in the charter business in 1985. Furthermore, the significant drop in gross receipts experienced by Mr. Maule's

² See, footnote 1, supra.

business for 1987 has been plausibly explained by the petitioner as occurring due to a PCB scare affecting the market for charter fishing services during that year. This explanation remains unchallenged by the respondent to any extent.

An examination of the factors detailed in Treas. Reg. § 1.183-2(b)(8) and (9), "the financial status of the taxpayer" and "elements of personal pleasure or recreation," respectively, favors the petitioner because the Maules did not realize substantial income or capital from any source other than Mr. Maule's salary with the Carnation Can Company. Further, the Maules utilized their boat for personal recreation on rare occasions compared to the level of charter use which is evident from the reported gross receipts of the business.

According to the 1986 expense summary for the Maules which was submitted with Sylvia Kahler's letter/affidavit, many thousands of dollars in out-of-pocket expenses were incurred by the Maules annually to operate the business in addition to the monthly payments made on the charter boat loan. The resulting picture is that of a rather inefficient, cash intensive method of sheltering Mr. Maule's modest salary from Carnation Can. It seems unlikely that Mr. Maule would seek to obtain comparatively small tax benefits at such a cost, when one considers the more likely inference that the investment was expected to yield profits at a later date.

Finally, during 1987 over 132 charter hire hours would have been required to generate the \$6,635 in gross receipts earned

by the business in that year, given the \$ 50.00 per hour rates charged by the Silly Girl Charter Service. Charter use required to support 1986 levels of gross receipts at \$ 50.00 per hour would have exceeded 400 hours. When one compares this level of charter use with the petitioner's uncontested recollection of four occasions on which the Maules used the boat for personal recreation, it becomes clear that personal use was de minimis.

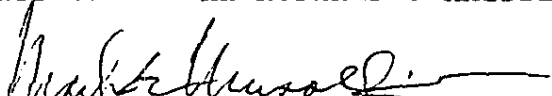
Therefore,

IT IS HEREBY ORDERED

That the petitioner's motion for partial summary judgment is granted and that the respondent's action on the petitioner's petition for redetermination is reversed.

Dated at Madison, Wisconsin, this 8th day of April, 1994.


WISCONSIN TAX APPEALS COMMISSION



Mark E. Musolf, Chairperson



Thomas R. Timken, Commissioner



Joseph P. Mettner, Commissioner

ATTACHMENT:
"Notice of Appeal Information"