

AUG 12 1999

STATE OF WISCONSIN

CIRCUIT COURT
BRANCH 1

DANE COUNTY

WISCONSIN DEPARTMENT OF REVENUE

Petitioner,

vs.

MEMORANDUM DECISION
AND ORDER

Case No.: 99 CV 0224

JOHNSON WELDING & MFG. CO., INC.
a/k/a JOHNSON TRUCK BODIES,
Respondent.

ADMINISTRATIVE AGENCY REVIEW

The matter before the court is Petitioner Wisconsin Department of Revenue's petition for review of a decision of the Tax Appeals Commission entered December 30, 1998, in Johnson Welding & Mfg. Co., Inc. v. Wisconsin Department of Revenue, Docket No. 97-S-252 (WTAC Dec. 30, 1998). On cross-motions for summary judgment, the Tax Appeals Commission ruled that Respondent's sales of twenty-five truck bodies were exempt from sales taxation under Wis. Stat. §77.54(5)(a), based on the finding that a nonresident corporation is a corporation that is incorporated outside of Wisconsin. After careful review, the court must reverse the decision of the Tax Appeals Commission.

BACKGROUND

The material facts of this case as adopted by the Tax Appeals Commission (Commission) are undisputed. Respondent Johnson Welding & Mfg. Co., Inc. (Johnson), has been engaged in the business of manufacturing and selling truck bodies in Rice Lake since 1931, which is its

principal place of business.

During the month of January 1997, Schwan's Sales Enterprises, Inc. (Schwan's) purchased twenty-eight truck bodies from Johnson. Schwan's has been Johnson's largest customer for many years. Schwan's took delivery of the truck bodies at Johnson's Rice Lake plant. Three of the truck bodies were installed on trucks assigned by Schwan's to depots in Wisconsin. The remaining twenty-five truck bodies were installed on trucks assigned by Schwan's to depots located in other states, and which would not be used by Schwan's in Wisconsin, other than in removing them from Johnson's plant in Rice Lake. When initial delivery was taken, the twenty-five trucks were all picked up and removed from Johnson's Rice Lake plant by a Schwan's driver to Schwan's principal place of business in Marshall, Minnesota, after which they were assigned to various non-Wisconsin locations.

Johnson charged Schwan's and collected 5.5% Wisconsin state and county sales tax on all twenty-eight truck bodies purchased by Schwan's, and remitted such taxes to the Wisconsin Department of Revenue (DOR). Based on information furnished to Johnson by Schwan's that twenty-five of the twenty-eight truck bodies were, after initial removal from Rice Lake to Schwan's location in Marshall, Minnesota, assigned by Schwan's to be used at depots located outside of Wisconsin, Johnson prepared and filed a claim for refund with the DOR seeking recovery of the January 1997 sales tax it had charged and collected from Schwan's with respect to the twenty-five non-Wisconsin destination truck bodies. Johnson's basis for seeking recovery of the sales tax was and is that the sales of the non-Wisconsin destination* truck bodies to Schwan's are exempt under §77.54(5)(a), Wis. Stats., because the sales at issue were made to a person, Schwan's, who is not a resident of Wisconsin and who will not use the trucks for

which the truck bodies were made otherwise than in their removal from Wisconsin.

Schwan's was incorporated under the laws of Minnesota on April 7, 1964, and has been continuously in existence and incorporated under the laws of Minnesota since that date. Its corporate headquarters are, and at all times during its existence have been, in Marshall, Minnesota.

Schwan's does business in all fifty states of the United States. Based on apportionment data derived from and used in preparing and filing its state corporate income and franchise tax returns, a comparison of the percentage of Schwan's sales, property, and payroll in Wisconsin as compared to its sales, property, and payroll outside Wisconsin for the three calendar years immediately preceding January 1997 is as follows:

	<u>1994</u>	<u>1995</u>	<u>1996</u>
PAYROLL			
% in WI	3.2343%	3.1743%	3.2439%
% outside WI	96.7657%	96.8257%	96.7561%
FIXED ASSETS (EXCLUDING RENT & INVENTORY)			
% in WI	2.5220%	2.4661%	2.5325%
% outside WI	97.4780%	97.5339%	97.4675%
SALES			
% in WI	3.7247%	3.7737%	3.7993%
% outside WI	96.2753%	96.2263%	96.2007%

The number of states in which Schwan's had higher dollar amounts than in Wisconsin for its payroll, fixed assets and sales for the three years immediately preceding the month of January

1997 is as follows:

	<u>1994</u>	<u>1995</u>	<u>1996</u>
Payroll	6	7	6
Fixed Assets	8	9	9
Sales	7	6	7

Schwan's has nineteen permanent business locations in Wisconsin, and operates 241 vehicles which are registered with the Wisconsin Department of Transportation. In the three years immediately preceding January 1997, the value of Schwan's Wisconsin property ranged from \$16.9 million to \$18.5 million. Its sales in the state for the same period were between \$66.6 million and \$74.2 million, while its payroll was between \$13.4 million and \$14.2 million. During the same three years, the company had between 822 and 907 Wisconsin employees.

In a letter dated April 2, 1997, the DOR denied Johnson's refund claim seeking recovery of the January 1997 sales tax it had charged and collected from Schwan's with respect to the twenty-five non-Wisconsin destination truck bodies. On April 11, 1997, Johnson filed with the DOR a Petition for Redetermination objecting to the denial of its refund claim. By Notice of Action dated May 27, 1997, the DOR denied Johnson's Petition for Redetermination on the basis that "[a] nonresident corporation is a corporation that is incorporated outside Wisconsin that does not have a place of business in Wisconsin."

On July 2, 1997, Johnson filed a Petition for Review with the Commission. The Commission ruled in favor of Johnson on a Motion for Summary Judgment, concluding that the sales of the twenty-five truck bodies to Schwan's were exempt from Wisconsin sales tax within the meaning of §77.54(5)(a), Wis. Stats., because Schwan's was not a resident of Wisconsin. The DOR now petitions this court for review of the Commission's decision.

STANDARD OF REVIEW

The scope of review for this court is found in § 227.57, Wis. Stats. This court must affirm the Commission's decision unless the court finds a basis for setting aside, remanding, or ordering agency action under a specific provision of § 227.57. Wis. Stat. § 227.57(2).

However, this court will reverse or remand a case to the agency if the agency's exercise of discretion is: (1) outside the range of discretion delegated to the agency by law; (2) inconsistent with an agency rule, an officially stated agency policy or a prior agency practice; or (3) otherwise in violation of a constitutional or statutory provision. Wis. Stat. §227.57(8); Barakat v. DHSS, 191 Wis. 2d 769, 782, 530 N.W.2d 392 (Ct. App. 1995). If the court finds the Commission has "erroneously interpreted a provision of law and a correct interpretation compels a particular action," the court shall set aside or modify the action. Wis. Stat. § 227.57(5). The court must accord due weight to the "expertise, technical competence, and specialized knowledge" of the Commission as well as "discretionary authority conferred upon it." Wis. Stat. § 227.57(10).

Although the court is not bound by the Commission's interpretations of law, Local No. 695 v. LIRC, 154 Wis. 2d 75, 82, 452 N.W.2d 368 (1990), the supreme court has set out the appropriate standards of review of an agency's legal and statutory interpretation:

This court has generally applied three levels of deference to conclusions of law and statutory interpretation in agency decisions. First, if the administrative agency's experience, technical competence, and specialized knowledge aid the agency in its interpretation and application of the statute, the agency determination is entitled to "great weight." The second level of review provides that if the agency decision is "very nearly" one of first impression it is entitled to "due weight" or "great bearing." The lowest level of review, the *de novo* standard, is applied where it is clear from the lack of agency precedent that the case is one of first impression for the agency and the agency lacks special expertise or experience in determining the question presented.

Jicha v. DILHR, 169 Wis. 2d 284, 290-91, 485 N.W.2d 256 (1992) (citations omitted).

DECISION

This case raises a question of law concerning the interpretation of §77.54(5)(a), Wis. Stats. Specifically, the issue is whether Schwan's, a corporation incorporated in Minnesota but

having business presence in Wisconsin, is a resident of Wisconsin for purposes of the sales tax exemption established in §77.54(5)(a). Section 77.54 exempts from general sales and use tax:

(5) The gross receipts from the sale of and the storage, use or other consumption of:

(a) . . . aircraft, motor vehicles or truck bodies sold to persons who are not residents of this state and who will not use such aircraft, motor vehicles or trucks for which the truck bodies were made in this state otherwise than in the removal of such aircraft, motor vehicles or trucks from this state.

Section 77.54(5)(a), Wis. Stats. Chapter 77 does not define "resident," and there have been no Wisconsin court cases interpreting the word "resident" as applied to a corporation for sales and use tax purposes under Wis. Stats. Ch. 77. However, the Commission did consider this precise question in K-C Aviation, Inc. v. WDOR, ¶ 400-052 (CCH) Wis. Tax Rptr. (WTAC 1994), wherein the Commission concluded as a matter of law that: (1) various corporations were not Wisconsin residents within the meaning of §77.54(5)(a) solely by reason of their doing business in Wisconsin as evidenced by holding a Wisconsin Seller's Permit and/or filing Wisconsin tax returns; and (2) that a corporation which had offices and/or employees in Wisconsin in addition to Wisconsin sales may be a Wisconsin resident within the meaning of §77.54(5)(a), depending on the nature and extent of its activities. In the case at hand, the Commission rejected the second conclusion reached by the Commission in K-C Aviation, characterizing this finding of law as a secondary conclusion unsupported by dictum. (Commission Decision at 8.)

The parties differ as to the appropriate standard governing this court's review of the Commission's decision. The DOR argues that the court should consider the Commission's decision *de novo* because there is no evidence of special agency experience with respect to the interpretation and application of §77.54(5)(a), and because the agency's position on the issue has

been inconsistent. Hacker v. DHSS, 197 Wis. 2d 441, 460-61, 541 N.W.2d 766 (1995); Coutts v. Wisconsin Retirement Board, 209 Wis. 2d 655, 664, 562 N.W.2d 917 (1997). Conversely, Johnson maintains that the court should afford great weight to the decision of the Commission and sustain its interpretation of §77.54(5)(a) because the Commission's decision is based on its expertise, competence and experience and has a rational basis.

While there is conflict between the Commission's decision in this case and in K-C Aviation, *supra*, the court finds that the Commission's position on the issue of corporate residency under §77.54(5)(a) has not been so inconsistent as to warrant *de novo* review. Instead, the court believes that "due weight" deference is appropriate because the Commission has some experience interpreting §77.54(5)(a) (K-C Aviation), but "has not developed the expertise which necessarily places it in a better position to make judgments regarding the interpretation of the statute than a court." Barron Elec. Coop. v. PSC, 212 Wis. 2d 752, 762, 569 N.W.2d 726 (Ct. App. 1997). Therefore, the court will sustain the Commission's interpretation if it is reasonable, even if another interpretation is equally reasonable, but will not do so if another interpretation is *more* reasonable than the one employed by the Commission. Id. at 763.

The Commission found Schwan's to be a non-resident of Wisconsin under §77.54(5)(a). This finding was based on the fact that Ch. 77 does not define "resident" and no specific provision exists in Ch. 77 which would include Schwan's as a Wisconsin "resident" for sales tax purposes. Absent such a provision, the Commission found Schwan's to be a non-resident irrespective of the extent of its Wisconsin presence. (Commission Decision at 9.)¹ The

¹Although the Commission's decision states that "[a]bsent such a provision, the petitioner, a Minnesota corporation, is a non-resident irrespective of the extent of its Wisconsin presence," the decision is clearly referring to Schwan's, and not Johnson Welding.

Commission declined to follow out of state cases which interpreted "resident" under similar sales tax exemption statutes to include foreign corporations with business presence in another state. Instead, because Wisconsin courts and the Wisconsin Board of Tax Appeals have interpreted the "residence" of a corporation to be its state of incorporation for income and franchise tax purposes, the Commission found Schwan's to be a non-resident of Wisconsin, and therefore exempt from the sales tax within the meaning of §77.54(5)(a).

In K-C Aviation, the only other case to consider the issue of residency under §77.54(5)(a), the Commission recognized that a corporation is generally considered a resident of its state of incorporation and no other, but it can be a resident of another state for some purposes, depending on its activities, and depending on local statutes to that effect. Based on the facts of that case, Commission found:

Under these circumstances, in the absence of statutory authority, respondent improperly determined that the questioned corporations were Wisconsin residents within the meaning of §77.54(5)(a), Stats., assuming such determination was based solely on the filing of Wisconsin tax returns showing sales in Wisconsin.

K-C Aviation, ¶ 400-052 at 30,194. The Commission then remanded the matter to the DOR to develop facts regarding the issue of residency, which was to be done so as to conform with the Commission's conclusions of law. One of the conclusions reached by the Commission was that a corporation which had offices and/or employees in Wisconsin in addition to Wisconsin sales may be a Wisconsin resident within the meaning of §77.54(5)(a), depending on the nature and extent of its activities. As mentioned above, the Commission in the case at hand rejected this conclusion, characterizing the finding of law as a secondary conclusion unsupported by dictum. However, the court does not believe that this finding by the Commission in K-C Aviation should be construed as dictum, because if indeed it was dictum, then it would not have been necessary

to remand the matter back to the DOR for further determination on the issue of residency. Instead, the court finds the conclusion reached in K-C Aviation relating to the interpretation of "resident" under §77.54(5)(a) to be an integral part of the Commission's decision, and maintains that it is agency precedent.

K-C Aviation opened the door to the possibility that a foreign corporation could be considered a Wisconsin resident within the meaning of §77.54(5)(a), depending on the nature and extent of its activities in Wisconsin. Respondent Johnson asserts that the meaning of the term "resident" as applied to a corporation is thoroughly established in Wisconsin law to mean the state of incorporation, and it must be presumed that the legislature knew of such meaning and used the word deliberately. The Commission based its decision on a similar rationale, stating that "[i]f there is to be an entirely different definition of a 'resident' corporation for sales tax purposes, the legislature must enact it or, at a minimum, acquiesce in an administrative rule so defining it." (Commission Decision at 10.)

However, while for Wisconsin income tax purposes a corporation is a resident of its domiciliary state, the court sees no reason to assume that the legislature intended to adopt this definition of corporate residence when it created §77.54(5)(a), an exemption to sales and use taxes based on non-residence. While it may not be unreasonable for the Commission to adopt the definition of corporate residency used in the income tax statutory scheme, the court believes it is *more* reasonable to determine residency for purposes of sales tax exemptions under §77.54(5)(a) based on the nature and extent of business activities in Wisconsin, particularly in light of the fact that agency precedent established in K-C Aviation clearly contemplates the possibility that foreign corporations could be treated as residents under §77.54(5)(a). "Resident"

may not explicitly be defined in Ch. 77, but K-C Aviation makes it clear that a corporation domiciled in another state can be considered a resident under §77.54(5)(a), depending on the extent and nature of its activities.

In addition, §77.54(5)(a) is a tax exemption statute, and such statutes, being matters of legislative grace, are strictly construed against granting the exemption. Ramrod, Inc. v. Dept of Revenue, 64 Wis. 2d 499, 504, 219 N.W.2d 604 (1974). As stated in the Commission's decision:

One who claims an exemption has the burden of showing that the property is clearly within the terms of the exception. Doubts are resolved against the exemption and in favor of taxability. Revenue Dept. v. Greiling, 112 Wis. 2d 602, 605 (1983). However, the interpretation of an exemption need not be unreasonable or the narrowest possible. Columbia Hospital Assoc. v. Milwaukee, 35 Wis. 2d 660, 668 (1967).

(Commission Decision at 6.)

While doubts are to be resolved against the exemption and in favor of taxability, the Commission's interpretation of the term "resident" as used in §77.54(5)(a) tends to do just the opposite. The Commission has construed the residency of a corporation to mean only those companies that are incorporated in the state of Wisconsin, regardless of the nature and extent of the companies' business activities in the state. However, it is far from clear who exactly falls under the §77.54(5)(a) non-resident exemption, and any doubts as to whether the tax exemption applies are to be resolved in favor of taxability. Revenue Dept. v. Greiling, 112 Wis. 2d at 605. Yet by interpreting corporate "resident" in such a limited manner, the Commission has essentially turned on its head the rule that tax exemption statutes be strictly construed against granting the exemption. Instead of resolving any doubts surrounding the meaning of "resident" corporation in favor of taxability, the Commission's interpretation of "resident" instead creates

a presumption that any non-domiciliary corporation is exempt from sales and use taxes under §77.54(5)(a), without regard to the nature and extent of business activities in Wisconsin.

The Commission's interpretation of corporate "resident" notwithstanding, the fact remains that §77.54(5)(a) is silent on the precise definition of "resident." The court has already concluded that, while it was not unreasonable for the Commission to adopt the definition of corporate residency used in the income tax statutory scheme, it is more reasonable to determine residency for purposes of sales tax exemptions under §77.54(5)(a) based on the nature and extent of business activities in Wisconsin, particularly in light of the Commission's holding in K-C Aviation. Likewise, following the statutory rule of strictly construing tax exemption statutes against the granting of the exemption, the court also determines that it is more reasonable to adopt a more expansive definition of corporate "resident" under §77.54(5)(a), one which considers the business presence of non-domiciliary corporations and resolves any doubts in favor of taxability. The term "resident" is a malleable term, and the Commission's own decision recognizes that a corporation can be considered a resident of a state other than its state of incorporation for some purposes, depending on its activities there and depending on local statutes to that effect. (Commission Decision at 8.) This recognition, combined with the strict construction of the §77.54(5)(a) sales tax exemption and the Commission's holding in K-C Aviation, reinforces the court's finding that it is more reasonable to interpret residency for non-domiciliary corporations based on the nature and extent of business activities in Wisconsin, rather than solely based on its state of incorporation.

In closing, the court must decide the specific issue of whether Schwan's is a resident of Wisconsin within the meaning of §77.54(5)(a), which depends on the nature and extent of

Schwan's business activities in Wisconsin. For the three calendar years preceding the month of January 1997, Schwan's had a Wisconsin workforce of between 822 and 907 employees, its Wisconsin payroll was between \$13.4 million and \$14.2 million, and its sales in the state were between \$66.6 million and \$74.2 million. During the same period, the value of Schwan's Wisconsin property ranged from \$16.9 million and \$18.5 million. Based on these circumstances, as well as other data outlined in the Commission's decision (*see* Commission Decision at 2-4), the court concludes that the nature and extent of Schwan's business activities in Wisconsin are such that Schwan's is a resident within the meaning of §77.54(5)(a). Therefore, Johnson's sales of twenty-five truck bodies to Schwan's are not exempt from sales taxation under Wis. Stat. §77.54(5)(a).

CONCLUSION

Therefore, for the reason stated above, the court must reverse the decision of the Tax Appeals Commission.

IT IS SO ORDERED.

Dated this 11 day of August, 1999.

BY THE COURT:



Honorable Robert A. DeChambeau
Circuit Court, Branch 1