STATE OF WISCONSIN

TAX APPEALS COMMISSION

INTERSYSTEMS CORPORATION,

Petitioner,

v.

WISCONSIN DEPARTMENT OF REVENUE,

Respondent.

DOCKET NO. 20-W-174

RULING AND ORDER

JESSICA ROULETTE, COMMISSIONER:

This case comes before the Tax Appeals Commission ("the Commission") for decision on competing Motions for Summary Judgment. The Petitioner, InterSystems Corporation, is represented in this matter by Attorneys John T. Barry, James E. Goldschmidt, and Nathan J. Oesch of Quarles & Brady, LLP. The Respondent, the Wisconsin Department of Revenue ("the Department"), is represented by Attorneys Mark Zimmer and Kasey Reese.

The parties filed a Joint Stipulation of Facts with attached Exhibits 1 through 20. Petitioner has filed a Motion for Summary Judgment, with a Supporting Brief and Supporting Affidavit with attached Exhibits 1 through 3, as well as a Brief in Response to the Department's Motion for Summary Judgment, with Exhibits 1 through 3 attached. The Department has filed a Motion for Summary Judgment with a Supporting Brief and two Supporting Affidavits with attached Exhibits M through P, as well as a

Brief in Response to Petitioner's Motion for Summary Judgment with an additional Supporting Affidavit with attached Exhibit 31. The Commission grants the Department's Motion for Summary Judgment and denies Petitioner's Motion for Summary Judgment.

ISSUE

Must InterSystems apportion the income it received from the licensing of its Caché computer software to Wisconsin, or is income InterSystems receives from the licensing of its Caché software properly excluded from Wisconsin income in the apportionment factor?

FACTS

Procedural Facts

1. InterSystems did not complete updated Form 5S, Form PW-1, and Form 1-NPR for the tax years at issue, 2010 through 2017, inclusive. (Joint Stipulation of Facts ("JSOF"), ¶ 57.)

2. On December 12, 2017, the Department initiated a technical review by a Request for Technical Review. (JSOF, ¶¶ 53, 54; Petition, Ex. B.)

3. On December 3, 2018, the Department announced by letter the results of its technical review. (JSOF, ¶ 56; Petition Ex. D.)

4. On April 22, 2019, the Department issued a separate Notice of Office Audit Amount Due - Pass-Through Withholding for each year from January 1, 2010, through December 31, 2017, (the "Audit Period"). (JSOF, ¶¶ 51, 58; Petition, Ex. A.)

5. On June 20, 2019, InterSystems mailed a letter to the Department which was a timely Request for Redetermination[1] of the April 22, 2019, assessments for each year of the Audit Period. (JSOF, ¶ 59; Petition, Ex. E.)

6. On May 7, 2020, the Department notified InterSystems by email that the Resolution Officer's final determination of InterSystems' Request for Redetermination was that the Request was denied. (JSOF, ¶ 67; Petition, Ex. I.)

7. On June 11, 2020, the Department issued a Notice of Action formally denying InterSystems' Request for Redetermination. (JSOF, ¶ 69; Petition, Ex. K.)

8. On July 22, 2020, InterSystems placed on deposit with the Department the full amount of the assessment, including interest, pursuant to Wis. Stat. § 71.90. (JSOF, ¶ 71.)

9. On August 10, 2020, InterSystems timely petitioned the Wisconsin Tax Appeals Commission for review of the Department's June 11, 2020, Notice of Action. (Commission file.)

10. On September 9, 2020, the Department timely answered InterSystems' petition. (Commission file.)

11. On February 16, 2022, the Commission granted InterSystems' unopposed Motion to Amend Exhibit F to the August 10, 2020, Petition. (Commission file.)

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[1] The parties refer to this as a "formal appeal." For clarity, the Commission will use the language of the Wisconsin Statutes throughout this ruling as the statutes denote the various stages of the review process.

Substantive Facts

InterSystems' software, Caché

12. InterSystems is a Massachusetts corporation specializing in creating database management system software, called Caché, that third parties use to create applications and manage information within those applications, primarily in the healthcare field. (JSOF, ¶¶ 1, 2.)

13. InterSystems contracts with third parties ("Application Partners" or "APs") that develop software applications using Caché and deliver those software applications, which utilize Caché, to their customers, referred to as "end user customers" in InterSystems' contracts with its APs. (JSOF, ¶ 3.)

14. Caché is used by the APs' software developers as a programming language or application development environment (i.e., as a tool for developing specific software applications) and by end user customers as a database management system to operate applications created by APs. (JSOF, ¶ 4.)

15. InterSystems' website, as of December 13, 2024, described Caché as "a high-performance database that powers transaction processing applications around the world. It is used for everything from mapping a billion stars in the Milky Way, to processing a billion equity trades in a day, to managing smart energy grids." (JSOF, ¶ 5.)

16. InterSystems provides support to APs for applications that work with Caché, and to end users. (JSOF, ¶ 6.)

17. InterSystems authorizes APs to use Caché for internal development. When an AP uses Caché for internal development, the AP is authorized by InterSystems to develop software applications that utilize Caché's programming language and to demonstrate Caché, and its functionality in connection with the software application the AP has developed, to potential end user customers. (JSOF, ¶¶ 7, 8.)

18. InterSystems also authorizes APs to offer end user customers the right to use Caché solely to operate the AP's application pursuant to the terms of an agreement between InterSystems and the end user customer. The end user customer is not permitted to use Caché in any manner not authorized by InterSystems. (JSOF, ¶ 9.)

InterSystems' relationship with Epic

19. Epic Systems Corporation ("Epic") has been one of InterSystems' APs since the late 1980s. (JSOF, ¶ 10.)

20. Epic creates and licenses software that is widely used in the healthcare community, including by hospitals, clinics, medical research facilities and other organizations that are responsible for providing medical care to patients. (JSOF, ¶ 11.)

21. Certain Epic software applications depend upon InterSystems' Caché to manage the large repositories of patient-related data accessed by those applications. (JSOF, ¶ 12.)

22. InterSystems has authorized Epic to use Caché for internal development of software applications dependent upon Caché and to demonstrate these software applications to potential end user customers. (JSOF, ¶ 13.)

23. InterSystems provides support to end user customers in conjunction with Epic software applications dependent upon Caché. Generally, end user customers contact Epic for support, and Epic contacts InterSystems as needed to provide support. (JSOF, ¶ 14.)

24. InterSystems' relationship with Epic is governed by the parties' Application Partner Agreements and Application Partner Profiles, as the parties have interpreted and applied those written agreements in the course of their relationship with one another since the late 1980s. (JSOF, ¶ 15.)

25. There were two Application Partner Agreements in place during the Audit Period: 1) the InterSystems Application Partner Agreement, "InterSys 001044-45," hereinafter the "2010 APA," which was in effect from January 1, 2010, through October 16, 2016, of the Audit Period, and 2) the InterSystems Amended and Restated Application Partner Agreement, "InterSys 001046-52," hereinafter the "2016 APA," which was in effect from October 17, 2016, through the end of the Audit Period, December 31, 2017. (JSOF, ¶¶ 16, 17, Exs. 1, 2)

26. There were two Application Partner Profiles in place during the Audit Period: 1) the InterSystems Application Partner Profile, "InterSys 001037-43," hereinafter the "2010 Partner Profile," which was in effect from January 1, 2010, through

October 16, 2016, and 2) the InterSystems Application Profile, "InterSys 001017-36," hereinafter the "2016 Partner Profile," which was in effect from October 17, 2016, through the end of the Audit Period, December 31, 2017. (JSOF, ¶¶ 18, 19, Exs. 3, 4.)

27. The 2010 Partner Profile is a part of the 2010 APA, and the 2016 Partner Profile is a part of the 2016 APA. (JSOF, ¶ 20, Exs. 1, 2, 3, 4.)

28. The way in which InterSystems authorized use of Caché by end user customers did not change throughout the Audit Period, notwithstanding any changes in the language between the 2010 and 2016 APA, and/or the 2010 and 2016 Partner Profile. (JSOF, ¶ 21.)

29. While Caché is used in conjunction with Epic's software, it is separate and distinct from Epic's software, though it may appear otherwise to end users as described in paragraph 43. (JSOF, ¶ 22.)

30. InterSystems has granted Epic as an AP the right to use Caché in developing Epic's own software applications, such that Epic's software application can run in conjunction with Caché, pursuant to an internal development license, "InterSys 1033." (JSOF, ¶ 23, Ex. 5.)

31. To the extent Epic pays InterSystems for Epic's use of the internal development license, the parties agree that this revenue should be sourced to Wisconsin for income tax and franchise tax purposes. (JSOF, ¶ 24.)

32. InterSystems fulfills orders for application-specific licenses for Caché by issuing a license key. (JSOF, ¶ 25.)

33. When (and only when) an Epic application dependent on Caché is to be delivered to an end user customer, Epic orders for that end user customer an application-specific license for Caché from InterSystems. (JSOF, ¶ 26.)

34. For each application-specific license, InterSystems produces a license key that is unique to the end user customer. (JSOF, ¶ 27.)

35. The license key specifies the license size (number of concurrent users authorized to use Caché at the same time) and other particular limitations. (JSOF, ¶ 28.)

36. The license key must be present on the end user customer's system in order for the end user customer to operate Caché with Epic's application. (JSOF, ¶ 29.)

37. License keys issued by InterSystems for end user customers of Caché in conjunction with Epic software dependent on Caché are provided to Epic for delivery to the end user customer. (JSOF, ¶ 30.)

38. The license key, which restricts the end user customer from using Caché in any way not authorized by InterSystems, may be installed on the end user customer's system by either Epic or the end user customer itself. (JSOF, ¶¶ 31, 32.)

39. When using Epic software dependent on Caché, an end user customer does not have to separately log in to Caché because the Epic software dependent on Caché will not operate without a valid end user license key issued to the end user customer and Caché will ensure that the end user customer has not exceeded the number of concurrent users authorized to use Caché at the same time. (JSOF, ¶ 33.)

40. End user customers' software or IT departments would be aware of and see Caché as distinct from Epic's software dependent on Caché, and InterSystems participates in annual meetings with those individuals for the purpose of sharing updates and answering technical questions. (JSOF, ¶ 34.)

41. InterSystems only issues license keys as and when requested by end user customers; Epic does not "warehouse" any application-specific licenses for Caché. (JSOF, ¶ 35.)

42. End users of Epic's software dependent on Caché did not make payments directly to InterSystems. (JSOF, ¶ 36.)

43. InterSystems does not receive any revenue for an application-specific license until, among other things, Epic has secured a sale of its application to an end user customer, placed an order with InterSystems for an application-specific license for Caché, and InterSystems has accepted such order and has issued a license key for such application-specific license to the end user customer through Epic. (JSOF, ¶ 37.)

44. During the Audit Period, Epic remitted to InterSystems a license fee for each license key for Caché that InterSystems issued to end user customers of Caché in conjunction with Epic's software applications dependent on Caché. These license fees were remitted by Epic to InterSystems on behalf of end user customers after InterSystems issued the associated license keys for Caché. (JSOF, ¶ 38.)

45. InterSystems invoiced Epic for the license fees due from end user customers for license keys for Caché. InterSystems did not issue invoices directly to the end user customers of Epic's software that was dependent on Caché. (JSOF, ¶ 39.)

46. Epic determined the price to its end user customers of the license fees due to Epic for its applications that were dependent on Caché. Epic was entitled to retain any remainder in excess of the amounts Epic owed and remitted to InterSystems. (JSOF, ¶ 40.)

47. Epic did not owe InterSystems an accounting of any remainder in excess of the amounts Epic owed and remitted to InterSystems. (JSOF, ¶ 41.)

48. Epic determined the markets in which it would sell or license Epic's software, including Epic's software that was dependent on Caché, but InterSystems retained the right to reject any order submitted by Epic. (JSOF, ¶ 42.)

49. During the Audit Period, Wisconsin end user customers represented between 3.10% and 7.53% of the total number of end user customers granted application-specific licenses for Caché, as follows:

- 2010: 6.55%
- 2011: 5.99%
- 2012: 5.97%
- 2013: 7.53%
- 2014: 4.75%
- 2015: 5.47%
- 2016: 3.91%
- 2017: 3.10% (JSOF, ¶ 43.)

InterSystems' relationship with end-user customers

50. Before an end-user customer receives an InterSystems license key, that end-user customer must agree to the InterSystems Caché Software Addendum, "InterSys 001012-16," hereinafter the "Caché Addendum," and was required to so agree at all times throughout the Audit Period. (JSOF, ¶¶ 44 - 46, Ex. 6.)

51. If end-user customers of Caché in conjunction with Epic software applications dependent on Caché had concerns or requested changes to the Caché Addendum, Epic would seek InterSystems' approval and InterSystems could accept, reject, or propose additional changes to the Caché Addendum. Typically, end-user customers of Caché in conjunction with Epic software applications dependent on Caché accepted the Caché Addendum without modification. (JSOF, ¶ 47.)

52. InterSystems relies on Epic to ensure that end-user customers agree to the Caché Addendum as InterSystems requires before issuing license keys. (JSOF, ¶ 48.)

53. Epic's applications that work with Caché would not function properly if the Caché Addendum was not accepted by the end-user because the end-user would not be permitted to use Caché. (JSOF, ¶ 49.)

54. Epic was not authorized to sublicense Caché separately. (JSOF, ¶ 50.)

APPLICABLE LAW

APPLICABLE PROCEDURAL LAW

Wis. Stat. 802.08 Summary judgment.
(1) Availability. A party may. . . move for summary judgment on any claim, counterclaim, cross claim, or 3rd-party claim which is asserted by or against the party. . . .
(2) Motion. . . . The judgment sought shall be rendered if the pleadings, depositions, answers to interrogatories, and admissions on file, together with the affidavits, if any, show that there is no genuine issue as to any material fact and that the moving party is entitled to a judgment as a matter of law.
. . .
(3) Supporting papers. Supporting and opposing affidavits shall be made on personal knowledge and shall set forth such evidentiary facts as would be admissible in evidence. Copies of all papers or parts thereof referred to in an affidavit shall be attached thereto and served therewith, if not already of record. The court may permit affidavits to be supplemented or opposed by depositions, answers to interrogatories, or further affidavits. When a motion for summary judgment is made and supported as provided in this section, an adverse party may not rest upon the mere allegations or denials of the pleadings but the adverse party's response, by affidavits or as otherwise provided in this section, must set forth specific facts showing that there is a genuine issue for trial. If the adverse party does not so respond, summary judgment, if appropriate, shall be entered against such party. . . .

APPLICABLE SUBSTANTIVE LAW

CHAPTER 71 INCOME AND FRANCHISE TAXES FOR STATE AND LOCAL REVENUES

SUBCHAPTER I TAXATION OF INDIVIDUALS AND FIDUCIARIES

Wis. Stat. 71.25 Situs of income; allocation and apportionment. For purposes of determining the situs of income under this section and s. 71.255 (5) (a) 1. and 2.:
. . . .

(5) Corporations engaged in business both within and without the state.

(a) *Apportionable income.* Except as provided in sub. (6), corporations engaged in business both within and without this state are subject to apportionment. Income gain or loss from the sources listed in this paragraph is presumed apportionable as unitary or operational income or other income that has a taxable presence in this state. Apportionable income includes all income or loss of corporations, other than nonapportionable income as specified in par. (b), including, but not limited to, income, gain or loss from the following sources:

. . .

6. Royalties from intangible assets.

. . .

10. Sale of intangible assets if the operations of the company in which the investment was made were unitary with those of the investing company, or if those operations were not unitary but the investment activity from which that gain or loss was derived is an integral part of a unitary business and the companies were neither affiliates nor related as parent company and subsidiary. . . .

. . . .

(6) Allocation and separate accounting and apportionment formula. Corporations engaged in business within and without the state shall be taxed only on such income as is derived from business transacted and property located within the state. The amount of such income attributable to Wisconsin may be determined by an allocation and separate accounting thereof, when the business of such corporation within the state is not an integral part of a unitary business, but the department of revenue may permit an allocation and separate accounting in any case in which it is satisfied that the use of such method will properly reflect the income taxable by this state. In all cases in which allocation and separate accounting is not permissible, the determination shall be made in the following manner: for all businesses . . . (a) there shall first be deducted from the total net income of the taxpayer the part thereof (less related expenses, if any) that follows the situs of the property or the residence of the

recipient. The remaining net income shall be apportioned to this state by use of the following:

. . .

(d) For taxable years beginning after December 31, 2007, an apportionment fraction composed of the sales factor under sub. (9).

(e) . . . For taxable years beginning after December 31, 2007, the apportionment fraction for the remaining net income of a financial organization is composed of a sales factor, as determined by rule by the department.

(6m) Apportionment formula computation.

(a)

. . .

2. For taxable years beginning after December 31, 2007, if both the numerator and the denominator of the sales factor under sub. (9) related to a taxpayer's remaining net income are zero, none of the taxpayer's remaining net income is apportioned to this state.

(b)

. . .

2. For taxable years beginning after December 31, 2007, if the numerator of the sales factor under sub. (9) related to a taxpayer's remaining net income is a negative number and the denominator of the sales factor under sub. (9) related to a taxpayer's remaining net income is a positive number, a negative number, or zero, none of the taxpayer's remaining net income is apportioned to this state.

(c)

. . .

2. For taxable years beginning after December 31, 2007, if the numerator of the sales factor under sub. (9) related to a taxpayer's remaining net income is a positive number and the denominator of the sales factor under sub. (9) related to a taxpayer's remaining net income is zero or a negative number, all of the taxpayer's remaining net income is apportioned to this state.

. . . .

(9) Sales factor. For purposes of sub. (5):

(a) The sales factor is a fraction, the numerator of which is the total sales of the taxpayer in this state during the tax period, and the denominator of which is the total sales of the taxpayer everywhere during the tax period. . . . For purposes of applying pars. (b) 2m. and 3. and (c), if a taxpayer is within another state's jurisdiction for income or franchise tax purposes for any part of the taxable year, it is considered to be within that state's jurisdiction for income or franchise tax purposes for the entire taxable year.

. . .

(df)

1. Gross receipts from the use of computer software are in this state if the purchaser or licensee uses the computer software at a location in this state.

2. Computer software is used at a location in this state if the purchaser or licensee uses the computer software in the regular course of business operations in this state, for personal use in this state, or if the purchaser or licensee is an individual whose domicile is in this state. If the purchaser or licensee uses the computer software in more than one state, the gross receipts shall be divided among those states having jurisdiction to impose an income tax on the taxpayer in proportion to the use of the computer software in those states. To determine computer software use in this state, the department may consider the number of users in each state where the computer software is used, the number of site licenses or workstations in this state, and any other factors that reflect the use of computer software in this state.

. . . .

(dj)

1. Except as provided in subd. 2m. and par. (df), gross royalties and other gross receipts received for the use or license of intangible property, including patents, copyrights, trademarks, trade names, service names, franchises, licenses, plans, specifications, blueprints, processes, techniques, formulas, designs, layouts, patterns, drawings, manuals, technical know-how, contracts, and customer lists, are sales in this state if any of the following applies:

a. The purchaser or licensee uses the intangible property in the operation of a trade or business at a location in this state. Except as provided in subd. 2m., if the purchaser or licensee

uses the intangible property in the operation of a trade or business in more than one state, the gross royalties and other gross receipts from the use of the intangible property shall be divided between those states having jurisdiction to impose an income tax on the taxpayer in proportion to the use of the intangible property in those states.

b. The purchaser or licensee is billed for the purchase or license of the use of the intangible property at a location in this state.

c. The purchaser or licensee of the use of the intangible property has its commercial domicile in this state.

. . . .

(dk) Sales of intangible property . . . are sales in this state if any of the following applies:

1. The purchaser uses the intangible property in the regular course of business operations in this state or for personal use in this state. If the purchaser uses the intangible property in more than one state, the sales shall be divided between those states having jurisdiction to impose an income tax on the taxpayer in proportion to the use of the intangible property in those states.

2. The purchaser is billed for the purchase of the intangible property at a location in this state.

3. The purchaser of the intangible property has its commercial domicile in this state.

. . . .

(15) Partnerships and limited liability companies.

(a) A general or limited partner's share of the numerator and denominator of a partnership's apportionment factors under this section are included in the numerator and denominator of the general or limited partner's apportionment factors under this section.

(b) If a limited liability company is treated as a partnership, for federal tax purposes, a member's share of the numerator and denominator of a limited liability company's apportionment factors under this section are included in the numerator and denominator of the member's apportionment factors under this section.

. . . .

CHAPTER 402 UNIFORM COMMERCIAL CODE - SALES

. . . .

SUBCHAPTER III GENERAL OBLIGATION AND CONSTRUCTION OF CONTRACT

Wis. Stat. 402.313 Express warranties by affirmation, promise, description, sample.

(1) Express warranties by the seller are created as follows:

(a) Any affirmation of fact or promise made by the seller to the buyer which relates to the goods and becomes part of the basis of the bargain creates an express warranty that the goods shall conform to the affirmation or promise.

(b) Any description of the goods which is made part of the basis of the bargain creates an express warranty that the goods shall conform to the description.

(c) Any sample or model which is made part of the basis of the bargain creates an express warranty that the whole of the goods shall conform to the sample or model.

(2) It is not necessary to the creation of an express warranty that the seller use formal words such as "warrant" or "guarantee" or that the seller have a specific intention to make a warranty, but an affirmation merely of the value of the goods or a statement purporting to be merely the seller's opinion or commendation of the goods does not create a warranty.

ANALYSIS

Under Section 802.08 of the Wisconsin Statutes, summary judgment shall be granted if the pleadings, depositions, answers to interrogatories, and admissions on file together, with the affidavits, if any, show that there is no genuine issue as to any material fact and that the moving party is entitled to a judgment as a matter of law. Where a party opposing summary judgment fails to respond or raise an issue of material fact,

the trial court is authorized to grant summary judgment. *Board of Regents v. Mussallem*, 94 Wis. 2d 657, 673-74 (1980).

Assessments made by the Department are presumed to be correct, and the burden is on each petitioner to prove by clear and satisfactory evidence in what respects the Department erred in its determination. *Edwin J. Puissant, Jr. v. Wis. Dep't of Revenue*, Wis. Tax Rptr. (CCH) ¶ 202-401 (WTAC 1984); Wis. Stat. § 77.59(1). Tax exemptions, deductions, and privileges are matters of legislative grace and will be strictly construed against the taxpayer. *Fall River Canning Co. v. Dep't of Taxation*, 3 Wis. 2d 632, 637, 89 N.W.2d 203 (1958).

InterSystems is a Massachusetts corporate pass-through entity. It is required to pay a withholding tax on any Wisconsin income that is allocable to a nonresident partner or shareholder. It is undisputed that InterSystems has income from Wisconsin: the central question in this appeal is precisely how much of its income is properly sourced to Wisconsin in each of the eight years of the audit period. The income at issue in this appeal is derived from an InterSystems' product called "Caché," which is database management system software.[2]

Epic Systems Corporation ("Epic") is a Wisconsin corporation and is an Application Partner of InterSystems. Epic creates and licenses software for use by end-users, primarily in the healthcare community. As part of its business, Epic develops software under the terms of agreements it has entered into with InterSystems, which the

[2] JSOF ¶ 2.

parties call APAs and Partner Profiles. Under the APAs and Partner Profiles, Epic has a license to use Caché to develop Epic's software programs which programs themselves then depend upon Caché to function.

Income from direct licenses of computer software to licensees is sourced to Wisconsin when the licensee uses the software in Wisconsin, where "use" means that the licensee uses the software in the regular course of business operations in Wisconsin or for personal use in Wisconsin, or if the licensee is an individual whose domicile is in Wisconsin. Wis. Stat. § 71.25(9)(df). The parties agree that payment for the license of Caché to Epic by InterSystems for Epic's own use in developing Epic's software should be sourced to Wisconsin for income tax and franchise tax purposes.[3] The parties' agreement regarding the tax treatment of this income complies with the provisions of Wis. Stat. § 71.25(9)(df): Epic is a Wisconsin corporation using Caché (computer software) in the regular course of Epic's business operations in Wisconsin.

The dispute regarding the Department's assessment relates to income paid to InterSystems which is generated as part of Epic's sale of Epic's own software to end-users. For the income at issue, when an end-user buys Epic's software, the end-user is required as a part of that purchase to acquire the separate right to use Caché in order for the Epic software to function. The parties do not agree on how to characterize the transaction by which the end-user acquires the right to use Caché.

[3] JSOF ¶24.

The Department frames the transaction whereby the end-user acquires the right to use Caché as one where Epic sells a sublicense of Caché to its end-users. The Department's position is that Epic has a license from InterSystems, which it uses to create Epic's own software product for an end-user. When Epic sells its software to an end-user, it sells a sublicense for Caché as part of the sale of Epic software. Under the Department's analysis, Wis. Stat. § 71.25(9)(df)'s focus on the location of the end-user of the software is inapplicable to income derived from transactions involving software sold by Epic to end-users, because the end-users hold a sublicense from Epic for the use of Caché, and Wis. Stat. § 71.25(9)(df) sets out Wisconsin law only as it relates to licensors and licensees. The Department's position is based on the Court of Appeals holding in its ruling in the *Microsoft* case that, "[t]here was no direct relationship between [the software seller] and the end-users because the end-users did not purchase anything, including a license, from [the software seller]." *See Wisconsin Dep't. of Revenue v. Microsoft Corp.*, 2019 WI App 62, ¶ 32.

Petitioner's position is based on its focus on where software, developed by Epic using Caché, is used by end-users. Petitioner argues that the most relevant statutory section under Wisconsin law is Wis. Stat. § 71.25(9)(df), which focuses on where the "purchaser or licensee" uses the software. Petitioner argues that, just because each end-user passes its payment for Caché to InterSystems through Epic, the income from those sales is not Wisconsin income for purposes of the apportionment formula. Petitioner further argues that the Court of Appeals did not hold in *Microsoft* that Wis. Stat. §

71.25(9)(df) requires that a licensor receive income from a licensee in order for the relevant inquiry to be the location of the use of the software. The Commission understands the Court of Appeals to have held just that when it wrote "[t]o repeat, the exception in the statutory subpart . . ., [Wis. Stat.] § 71.25(9)(df), is limited to a 'licensee' who uses Microsoft's software in Wisconsin." *Microsoft* at ¶ 30. Petitioner uses reasoning in the Commission's decision in *Skechers USA, Inc. II v. Wis. Dep't of Revenue*, Wis. Tax Rptr. (CCH) ¶ 401-978 (WTAC 2015) to argue that the Commission should find in its favor in this appeal. However, the Commission is bound by the Court of Appeals' legal conclusions in the subsequently issued *Microsoft* decision, and so, to the extent that the Commission's reasoning in *Skechers II* contradicts the *Microsoft* ruling, the Commission considers its 2015 reasoning in *Skechers II* to have been overruled. Petitioner also argues that the Commission should follow the reasoning set forth in the Commission's Ruling and Order in the *Microsoft* case, which Ruling and Order was ultimately affirmed by the Court of Appeals, when the Commission focused on the fact that Microsoft's revenue did not flow "from the use of computer software." *Microsoft v. Wis. Dep't of Revenue*, CCH ¶ 402-162 (WTAC 2017). The Court of Appeals' ruling rendered that analysis by the Commission superfluous when it determined that Wis. Stat. § 71.25(9)(df) was inapplicable to the underlying transaction, because subsection (df) only applies to licensees. *Microsoft* at ¶ 30.

Accordingly, the Commission here begins with making a determination of whether or not end-users of Epic's software, developed using Caché, are licensees of

InterSystems. The Commission will quote rather extensively from the Court of Appeals opinion in *Microsoft*, because that case is controlling precedent on this issue.

> The pertinent statutes do not contain definitions of the common terms license, licensor, licensee, sublicense, or sublicensee. But, the meanings are well known, and neither party offers a different definition of these terms. A licensor grants a portion of its rights, such as intellectual property rights to software, to a licensee through a license. See BLACK'S LAW DICTIONARY 1061, 1062 (10th ed. 2014). A licensee may grant to another, through a sublicense, a portion or all of the rights granted to the licensee by the original license. See id. At 1652. The party holding a sublicense is known as a sublicensee. See WEBSTER'S THIRD NEW INTERNATIONAL DICTIONARY 2276 (1993).[4]

The Department argues that the end-users are "sublicensees" of InterSystems, making Wis. Stat. § 71.25(9)(df) inapplicable, because: 1) the Application Partner Agreements and Application Partner Profiles explicitly grant the right to Epic to sublicense Caché to end-users, as governed by the standard ISC addendum; 2) the Caché Addendum describes in detail the sublicensing agreement from the perspective of the Epic end-user, referred to in the Caché Addendum as "You;" 3) the heading of the Caché Addendum is "Exhibit A - Sublicense Terms;" 4) in numbered paragraph 1.a(i), InterSystems warrants that it has valid title to the Sublicensed Software, that it has the right to license Caché to Epic, and the right to license Epic to grant sublicenses to its end-user; 5) in numbered paragraph 4.e.(i) of the Caché Addendum, the end-user is prohibited from copying the Sublicensed Software, except for making a backup copy; 6)

[4] *Microsoft* at ¶ 24.

the agreement the end-user signs to use Caché is an agreement with Epic, not an agreement with InterSystems; 7) the Standard ISC Addendum grants limited rights to the end-user; 8) end-users paid the fees for their sublicenses to Epic; and 9) Epic determined the price of the sublicense granted to an individual end-user and was entitled to keep monies collected in excess of what was due to InterSystems for sublicenses.

Petitioner counters the Department's first eight arguments as follows: 1) the 2010 APP expressly states that "Epic is authorized to sell on behalf of InterSystems Corporation . . . the following Licenses and Services: Licenses: all Concurrent User Caché Enterprise Licenses,; the 2016 APP states that "Epic is authorized to offer (i) Licenses to use the following Licensed Software . . .: Licensed Software: Caché, Ensemble and certain HealthShare products;" and the fees paid for licenses granted to end-users are based on "the then-current price list for the country or region where the customer is located," where "customer" refers to the end-user; 2) where the Caché Addendum defines "Sublicensed Software," it says they are computer programs "licensed by InterSystems through Epic to You;" 3) the Caché Addendum refers to computer programs "licensed by InterSystems through Epic to You" despite the heading on the Addendum including the phrase "Sublicense Terms;" 4) and 5) while the Caché Addendum refers both to "licenses" and "sublicenses," the very inconsistency in the document itself requires the Commission to ignore the words chosen by Epic and InterSystems and instead analyze the substance of the relationships among Epic, InterSystems, and end-users; 6) InterSystems is a party to the relevant contract, and a contract does not require a signature

or written agreement, so long as there is meeting of the minds as to the essential terms of the agreement, and there is offer, acceptance, and consideration: the Caché Addendum becomes binding on the parties when an end-user places an order through Epic, InterSystems accepts that order and issues a license key, and the end-user pays for the license key; 7) InterSystems makes express representations and warranties to the end-user which are enforceable against InterSystems pursuant to Wis. Stat. § 402.313(1)(a); and 8) each license key is both uniquely tailored to each end-user and changes based on increased or decreased use. Petitioner's counterarguments focus on the case by case issuance of the sublicenses to the end-users and ask the Commission to reason that, because Epic did not have the authority to independently issue license keys, end-users had a direct relationship with InterSystems.

Petitioner affirmatively argues that end-users are "licensees" of InterSystems as that word is used in (df) because: 1) InterSystems receives income from the actual use of Caché when it is contained in Epic's software; 2) agreements between InterSystems and end-users use language that, as a whole, reflects a licensor-licensee relationship, and not a licensor-sublicensee relationship; 3) the Caché Addendum is a contract between InterSystems and the end-user, which includes express representations and warranties made by InterSystems to the end-user enforceable by the end-user against InterSystems pursuant to Wis. Stat. § 402.313(1)(a); 4) license keys issued by InterSystems to end-users are uniquely tailored and change based on increased or decreased use; 5) Epic does not warehouse license keys on behalf of InterSystems; 6) InterSystems receives

no income until an end-user is secured by Epic; and 7) the income InterSystems receives for license keys varies according to the end-user's use of Caché.

The Department responds to InterSystems' arguments as follows: 1) when Epic passes the cost of Caché through to the end-user as part of the cost of Epic's software, the pass-through of the cost does not transform the end-user into InterSystems' licensee; the moneys paid to InterSystems by Epic for end-users' use of Caché are not tied to the price of Epic's software; and Epic is entitled to keep the profits on the sales of Epic's software, including any amounts attributable to Caché; 2) there are no agreements between InterSystems and the end-users: in fact, the InterSystems Application Partner Profile at paragraph 5 states that InterSystems "will not provide a formal quote to, or otherwise license directly to, a known Epic customer or known Epic prospect for Caché Licenses or Services to run Epic applications without obtaining Epic's prior written consent;" 3) the Caché Addendum included language that provided that Epic, and not InterSystems, was responsible for product support and end-users should contact Epic in case of problems or questions regarding the software; 4) and 7) Epic, and not InterSystems, determined the price of license keys to end-users, Epic was entitled to retain end-user payments in excess of amounts Epic remitted to InterSystems, and Epic was not required to provide an accounting of the total amount of license key fees collected by Epic for Caché; 5) the warehousing of license keys is not relevant to a determination of whether end-users are sublicensees of InterSystems, because whether the license keys are ordered in bulk on a case by case basis does not change the fact that Epic was the

licensee of InterSystems; and 6) any business that provides sublicensing rights will have income that derives from the sales of those rights.

Following the reasoning of the Court of Appeals in *Microsoft*, the Commission examines the agreements among InterSystems, Epic, and the end-users to determine the nature of the relationship of the end-users to InterSystems. The end-user receives the Caché Addendum as part of the contract which the end-user signs when purchasing software from Epic. The Caché Addendum is not signed by a representative of InterSystems. No part of the purchase contract signed by an end-user is signed by InterSystems. InterSystems relies on Epic's representation to InterSystems that the Caché Addendum has been provided to an end-user prior to InterSystems' issuing a product key to an individual end-user. In order for an end-user to have a licensor-licensee relationship with InterSystems, the end-user must form a contract with InterSystems. Petitioner argues that the end-user accepts the Caché Addendum when it accepts the Epic sales contract in toto, and that InterSystems accepts the Caché Addendum when it accepts the Epic sales contract and issues a license key for the end-user's use of Caché. However, InterSystems admittedly does not track whether the Caché Addendum has been provided to the end-user by Epic. It is too much of a stretch to find that an addendum, which one "party" cannot know has been provided to another "party" constitutes proof of mutual assent to the end-user agreement (here, the Caché Addendum). Petitioner also argues that the express warranties contained in the Caché Addendum are further proof that InterSystems was selling a license to the end-user, because the end-user would be

unable to enforce those warranties in the absence of a contract between InterSystems and the end-user. The warranties provided for in Wis. Stat. § 402.313 are enforceable against the parties to a sale of goods. Petitioner's argument presumes that, if the Caché Addendum is not a sale of a license from InterSystems to an end-user, it is not a contract. However, this argument puts the cart before the horse. The argument could also be made that the Caché Addendum is enforceable against Epic, as the seller of the sublicense, should an end-user seek to prove the existence of and then enforce any warranties contained in the Caché Addendum. The Commission determines that no valid contract was formed between InterSystems and the end-users. Since there must be a contract in order for an end-user to have a licensor-licensee relationship with InterSystems, we must conclude that end-users of Epic's software, developed using Caché, are not licensees of InterSystems.

The Court of Appeals held that income Microsoft received from the computer sellers (Epic, in this appeal) was income from the sale of an intangible. *Microsoft* at ¶¶ 20 – 21. At the time the Court of Appeals was writing, this led to the application of the provisions of Wis. Stat. § 71.25(9)(d) in its analysis of how the income paid to Microsoft for the sublicenses granted to end-users should be apportioned. Since that time, the pertinent Wisconsin statutes have been amended. The Commission must now examine whether Wis. Stat. § 71.25(9)(dj), relating to income from royalties, or Wis. Stat. § 71.25(9)(dk), relating to income from sales of intangible property, is the appropriate

subsection to apply to the income InterSystems receives from Epic for the end-users' use of Caché as part of the end-users' purchase of Epic's software.

The Commission begins with the definition of "royalty" as it applies Wis. Stat. § 71.25(9)(dj) to the facts in this appeal. A "royalty" is a "Payment made to an author or inventor for each copy of a work or article sold under a copyright or patent." *Royalty,* BLACK'S LAW DICTIONARY *(8th ed. 2004)*. The treatment of income derived from a royalty payment is set forth in Wis. Stat. § 71.25(9)(dj). Under this subsection, gross royalties received for the use or license of intangible property are sales in Wisconsin if any of three factors are true: 1) the purchaser or licensee uses the intangible property in the operation of a trade or business at a location in Wisconsin; 2) the purchaser or licensee is billed for the purchase or license or use of the intangible property at a location in Wisconsin; or 3) the purchaser or licensee of the use of the intangible property has its commercial domicile in Wisconsin. The end-users neither purchase nor license Caché from InterSystems, so the first factor of this subsection does not resolve the dispute. Turning to the second factor, Epic is billed for the purchase and license, and eventual sublicense to end-users, of Caché at its headquarters in Wisconsin. Here, end-users can be argued to indirectly pay InterSystems for the use of Caché, particularly since the money sent to InterSystems increased as the numbers of users increased. However, the money sent to InterSystems by Epic was set according to a schedule known only to Epic and InterSystems. The record is clear that, were Epic to collect money in excess of the fee schedule between Epic and InterSystems, Epic could keep that excess without having to provide an accounting to

InterSystems. The Commission determines that Epic uses, in Wisconsin, its license to sublicense Caché to end-users. The income sent to InterSystems by Epic for the sublicenses granted to end-users is appropriately sourced as to Wisconsin as royalty income under the second factor of the applicable statute. Finally, as the purchaser and licensee of Caché, Epic's commercial domicile in Wisconsin leads to sourcing of the sublicense income to Wisconsin under the third factor of the statute as well.

Viewing the income paid by Epic to InterSystems as income from the sale "of intangible property, excluding securities" requires the application of Wis. Stat. § 71.25(9)(dk). Under this subsection, income received for the sales of intangible property are sales in Wisconsin if any of three factors are true: 1) the purchaser uses the intangible property in the regular course of business operations in Wisconsin; 2) the purchaser is billed for the purchase of the intangible property at a location in Wisconsin; or 3) the purchaser of the intangible property has its commercial domicile in this state. The end-user does not purchase Caché directly from InterSystems, so the first factor of this subsection does not resolve the dispute. Epic is billed by InterSystems for the purchase of Caché, and for the eventual purchase of sublicenses by end-users, at Epic's headquarters in Wisconsin. Accordingly, the income to InterSystems for the sublicenses purchased by end-users is appropriately sourced to Wisconsin under the second factor of the applicable statute. Finally, as the purchaser of Caché, Epic's commercial domicile in Wisconsin leads to sourcing of the sublicense income to Wisconsin under the third factor of the statute as well.

Petitioner raises a constitutional objection to Wis. Stat. §§ 71.25(9)(dj) and (dk) as those statutes are written. The Commission does not have the authority to find that a statute is unconstitutional on its face. *McManus v. Wisconsin Dep't of Revenue*, 155 Wis. 2d 450, 454, 455 N.W.2d 906 (Ct. App. 1990).

Petitioner continues on to claim that apportioning all income from Epic's sales of sublicenses to Wisconsin violates the Commerce Clause of the United States Constitution as Wis. Stat. §§ 71.25(9)(dj) and (dk) are applied in this appeal. Petitioner takes the position that, in order to comply with the Commerce Clause, a state tax must have a substantial nexus with the taxing state, be fairly apportioned, not discriminate against interstate commerce, and be fairly related to the services conducted in Wisconsin.

In assessing whether the tax is fairly apportioned, Petitioner applies the analytical tools laid out by the Supreme Court, by addressing "whether the tax is 'internally consistent' and, if so, whether it is 'externally consistent' as well." *Oklahoma Tax Comm'n v. Jefferson Lines, Inc.*, 514 U.S. 175, 185 (1995).

In order for a tax to survive analysis regarding internal consistency, the Commission must determine that if every state imposed a similarly structured tax, interstate and intrastate commerce would not be differently burdened. Petitioner argues that the structure of Wis. Stat. §§ 71.25(9)(dj) and (dk), were they enacted in every state of the union, would result in income being taxed by multiple jurisdictions, and so the application of these statutory subsections to Petitioner's income results in a violation of the Commerce Clause. The Department counters that application of Wis. Stat. §§

71.25(9)(dj) and (dk) does not source income to location inside and outside the state simultaneously, because by their very structure, the first prong that is applicable determines where the income should be sourced, resulting in single state sourcing for gross income. The Commission finds the Department's argument persuasive and determines that Wis. Stat. §§ 71.25(9)(dj) and (dk) do not fail an external consistency analysis as they are applied to Petitioner in this appeal.

In order for a tax to survive analysis regarding external consistency, the tax must have an economic justification for the State's claim on the value taxed, and the tax must not reach beyond that portion of value which is fairly attributed to economic activity within the state. Petitioner argues that the measure of economic activity within the state should be determined by the use of the sub-licenses. Turning again to the precedent set forth in the *Microsoft* case, the Department argues that Wisconsin is not taxing the use of the sub-licenses, it is taxing the economic activity of the sale of the sub-licenses, which happens in Wisconsin, where Epic, the licensee, concludes its sales of sub-licenses. The Commission finds the Department's argument persuasive and determines that Wis. Stat. §§ 71.25(9)(dj) and (dk) do not fail an internal consistency analysis as they are applied to Petitioner in this appeal.

Petitioner states that Epic obtains a license to use Caché for its own work in software development. Further, "InterSystems does not authorize Epic to use the application-specific license InterSystems grants to the end-user." Petitioner goes on to argue that, since the end-user pays for the right to use Caché to operate Epic's software,

which Epic is specifically prohibited from doing, any right obtained by the end-user to use Caché to operate Epic's software cannot be a sublicense from Epic, because Epic cannot issue a sublicense that includes a right that Epic does not hold. However, this argument mischaracterizes the plain meaning of the quoted phrase. The phrase pointed to by Petitioner as limiting Epic's rights under the license simply means that Epic must use its own Caché product key to operate Epic software sold to end-users: the prohibition is on the use of the product key granted to the end-user by Epic to operate Epic's software, nothing more and nothing less.

The Commission understands the frustration of Petitioner, which began its dispute with the Department in December 2017, almost two full years before the Court of Appeals issued its ruling in the *Microsoft* case. The Petitioner argues that the Department changed its position over the course of the parties' dispute, first applying (df), then later applying (dj) or (dk) to the income derived from the end-users' use of Caché. InterSystems calls this change in the Department's position a position of convenience and not of conviction. This characterization of the Department's action is unfair. The Department is bound by the ruling of the Court of Appeals, as are both InterSystems and the Commission. When the Department followed the interpretation of subsection (df) set forth by the Court of Appeals in 2019, it acted as a responsible state agency, showing respect for the rule of law. Given the time and money InterSystems invested in negotiations with the Department, its frustration is an understandable reaction. The

overlapping timing of the two appeals certainly made resolution of this appeal extremely difficult.

CONCLUSIONS OF LAW

1. There must be a contract in order for end-users of Epic's computer software to have a licensor-licensee relationship with InterSystems. There is no contract between end-users of Epic software and InterSystems, and so InterSystems does not license its computer software to the end-users of Epic's computer software. Wis. Stat. § 71.25(9)(df) is not applicable to determine the source of the income InterSystems derives from end-users of Epic's computer software.

2. Because the purchaser is billed for the intangible product at an address in Wisconsin, under both Wis. Stat. §§ 71.25(9)(dj) and (dk), the income InterSystems receives from Epic's customers for the use of its Caché software alongside Epic's software is properly sourced to Wisconsin.

3. As they are applied to Petitioner, Wis. Stat. §§ 71.25(9)(dj) and (dk) do not violate the Commerce Clause of the United State Constitution.

ORDER

The Department's Motion for Summary Judgment is granted, and InterSystems' Motion for Summary Judgment is denied.

Dated at Madison, Wisconsin, this 20th day of November, 2025.

WISCONSIN TAX APPEALS COMMISSION

Elizabeth Kessler, Chair

Jessica Roulette, Commissioner

Kenneth P. Adler, Commissioner

ATTACHMENT: **NOTICE OF APPEAL INFORMATION**

WISCONSIN TAX APPEALS COMMISSION
101 E Wilson St, 5th Floor
Madison, Wisconsin 53703

NOTICE OF APPEAL INFORMATION

NOTICE OF RIGHTS FOR REHEARING, OR JUDICIAL REVIEW, THE TIMES ALLOWED FOR EACH, AND THE IDENTIFICATION OF THE PARTY TO BE NAMED AS RESPONDENT

A taxpayer has two options after receiving a Commission final decision:

Option 1: PETITION FOR REHEARING BEFORE THE COMMISSION

The taxpayer has a right to petition for a rehearing of a final decision within 20 days of the service of this decision, as provided in Wis. Stat. § 227.49. The 20-day period commences the day after personal service on the taxpayer or on the date the Commission issued its original decision to the taxpayer. The petition for rehearing should be filed with the Tax Appeals Commission and served upon the other party (which usually is the Department of Revenue). The Petition for Rehearing can be served either in-person, by USPS, or by courier; however, the filing must arrive at the Commission within the 20-day timeframe of the order to be accepted. Alternately, the taxpayer can appeal this decision directly to circuit court through the filing of a petition for judicial review. It is not necessary to petition for a rehearing first.

AND/OR

Option 2: PETITION FOR JUDICIAL REVIEW

Wis. Stat. § 227.53 provides for judicial review of a final decision. Several points about starting a case:

1. **The petition must be filed in the appropriate county circuit court and served upon the Tax Appeal Commission and the other party (which usually is the Department of Revenue) either in-person, by certified mail, or by courier,** within 30 days of this decision if there has been no petition for rehearing or, within 30 days of service of the order that decides a timely petition for rehearing.
2. If a party files a late petition for rehearing, the 30-day period for judicial review starts on the date the Commission issued its original decision to the taxpayer.
3. The 30-day period starts the day after personal service, or the day we mail the decision.
4. **The petition for judicial review should name the other party (which is usually the Department of Revenue) as the Respondent, but not the Commission, which is not a party.**

For more information about the other requirements for commencing an appeal to the circuit court, you may wish to contact the clerk of the appropriate circuit court or, the Wisconsin Statutes. The website for the courts is *https://wicourts.gov*.
This notice is part of the decision and incorporated therein.